CHAPTER - ONE

INTRODUCTION

1.1 Background of the Study

To start with, performance in terms of profitability is a benchmark for any business enterprise including the banking industry. Extension of credit is one of the major activities of banks and financial institution. Credit represents the bulk of the bank and financial institution's asset portfolio. However, increasing NPAs have a direct impact on banks profitability as legally banks are not allowed to book income on such accounts and at the same time banks are forced to make provision on such assets as per the central bank guidelines. Also, with increasing deposits made by the public in the banking system, the banking industry cannot afford defaults by borrower s since NPAs affects the repayment capacity of banks. Further, central Bank successfully creates excess liquidity in the system through various rate cuts and banks fail to utilize this benefit to its advantage due to the fear of burgeoning non-performing assets.

Economic development is the foundation development of any country. Economic development is supported by the financial infrastructure of that country. Financial institution constitutes an important part of the financial infrastructure. The main function of the bank is the collection of idle funds and mobilizes them to productive sector causing overall economic development, which finally leads to national development of the country. Bank pools the fund through deposit and mobilize them to productive sector in the form of loans and advances. Bank is the financial institution which deals with money by accepting by accepting various types of deposits, disbursing loan and rendering various types of financial services. It is the intermediary between the deficit and surplus of financial sources.

It cannot be denied that the issue of development rest upon the mobilization of resources and the bank deals in process of channelizing the available resources in the needed sectors. Commercial bank collects deposits from the public and the largest portion of deposited funds is utilized by disbursing loan and advances. The balance sheet of a commercial bank reflects deposit constitutes a major portion of the liabilities and the loan and advances constitutes a major portion of the asset side. Similarly the profit of the bank depends upon the spreads that it enjoys between the interest it receive from the borrowers and that to be paid to the depositors. An average bank generates about 70% of its revenue through its lending. The return that the bank enjoys of deposit mobilization through loan and advances is very attractive but they do not come free of cost and free of risk. There is risk in lending. The bank faces number of risk like interest rate risk, liquidity risk, credit risk, borrower risk etc. Such risk in excessive form had led many banks to go bankrupt in number of countries.

Amongst many risk that bank faces one of the most critical is borrower risk – the risk of non payment of the disbursed loans. Failure to collect fund disbursed may sometimes results in the bank's inability to make repayment of the money to depositors and return to the shareholders. The bankers have the responsibility of safeguarding the interest of the depositors, shareholder and society they are serving. If bank behaves unresponsively the cost born by the economy is enormous. Banking sector is volatile and sensitive sectors of national economy, which require effective monitoring and efficient supervision. Smooth and effective operation of banking activities is most for sustainable economic growth of a country. The regulatory agency should always be watchful of banking activities carried out by government and non governmental banking and financial institution.

In the distant past, banks had to deal with only few cases of bad-loans. So, they used to take legal actions against chronic defaulters of bank-loans. For the last ten/twelve years, banks are suffering from a large chunk of non-performing loans (assets) as a consequence of economic as well as non-economic factors in the country. By international parameter, non-performing assets of a bank should not exceed ten percent while such an indicator is estimated to have been crossed 26 percent, (Rs. 31 billion in aggregate) mainly due to the increase in willful defaulters in the government, semi-government and private sector banks.

Recovery of bad loans by banks and financial institutions has turned into a big issue in the financial sector of Nepal. This has greatly caused negative impact upon Banks' profit, government revenue and the overall financial sector of the country. This calls for an effective system and mechanisms that case the early recovery of debts of banks and also of bank like institutions as specified by Nepal Rastra Bank the Monetary Authority.

Due to their control role in the economy, government and central bank try their best to rescue banks from such situations. Hence to protect the banks from such situation and protect depositors and shareholders interest, central bank issues various directives and guidelines from time to time with modification and amendments for the sound regulation of the banking system. All the banks have to abide by the rules and regulation issued by central bank of the country.

1.2 Focus of the Study

Bank disbursed loan and advances for certain predetermined periods or every loans and advances has its maturity period or expiry date and borrower must repay the loan by the maturity period but there is no certainty that all the loans are recovered by the maturity date. Some loans are recovered with in maturity period but some loans are not recovered even after its maturity period and remains as non-performing asset of the bank. Bank in Nepal are in poor health. Increasing non-performing asset of Nepalese banking sector is estimated to be 30%. Bank is facing problems in recovering the granted loans that had turned to non-performing asset. The nationalized two commercial bank named Nepal Bank Limited and Rastriya Banijya Bank have non-performing asset to the extent of 60% and 50% respectively. Nowadays, in most of national newspaper, it can be seen that government owned commercial bank are publishing names of borrower who defaulted in making payment of bank loans. Even the private and joint venture banks are facing the problem of increasing non-performing asset. This problem may lead to bankruptcy bank and failure of banking system adversely affecting the depositors and other parties of the society.

The origin of the problem of burgeoning NPAs lies in the quality of managing credit risk by the banks concerned. What is needed is having adequate preventive measures in place namely, fixing pre-sanctioning appraisal responsibility and having an effective post-disbursement supervision. Banks concerned should continuously monitor loans to identify accounts that have potential to become non-performing.

In order to rescue bank from the financial distress, to safeguard depositors interest to ensure stability in the economy, NRB issues directives from time to time related to various aspects of the banks. NRB directives number 2 (2001) is related to loan classification and provisioning of commercial banks. As per this directive commercial bank supposed to categorize the loan disbursed into four different categories on the basis of ageing of its past dues and each categories of loan require certain percentage of it to be provisioned for the probable loss. Going through the old directives regarding the loan loss provision, banks had classified loans into six categories and as per those directives, for a loan to be bad the time period of past due was 5 year. But with new directives, that period has also been reduced. This means the previously categorized substandard loan will now be a doubtful loan and a doubtful loan is bad loan. The provisioning amount is taken from by deducting from the profit of the bank. Hence there is great impact of loan loss provision in the profitability of the banks. The provision of the loan means the net profit of the bank will come down by that amount. Increase in loan loss provision decrease then profit of the bank leading to decrease in dividends to shareholders. However adequate loan loss provision strengthen the financial health of the banks by controlling credit rill and safeguards the depositors money leading to overall economic development of the country.

1.2.1 Profiles of the Banks under Study

In this section general introduction of the banks under study is being attempted to furnish for the easy reference of the samples to the research.

(i) Introduction to Nepal Investment Bank Ltd.

Nepal Investment Bank Ltd. (NIBL), previously Nepal Indosuez Bank Ltd., was established in 1986 as a joint venture between Nepalese and French partners. The French partner (holding 50% of the capital of NIBL) was Credit Agricole Indosuez, a subsidiary of one the largest banking group in the world. With the decision of Credit Agricole Indosuez to divest, a group of companies comprising of bankers, professionals, industrialists and businessmen, had acquired on April 2002 the 50% shareholding of Credit Agricole Indosuez in Nepal Indosuez Bank Ltd. The name of the bank has been changed to Nepal Investment Bank Ltd. upon approval of bank’s Annual General Meeting, Nepal Rastra Bank and Company Registrar’s office.

The head office of NIBL is at Durbar Marg, Kathmandu. NIBL has 41 branches as per report of FY 2010/11. NIBL visions is "Our Vision is to be the most preferred provider of Financial Services in Nepal" Its core values and ethical principles are customer focus, quality, honesty and integrity, belief in our people, teamwork, good corporate governance and corporate social responsibility.

The present share capital and ownership of NIBL is as follows:

1.	**Domestic Ownership**	**100.00 %**	**Rs. 2,40,90,97,700.00**
1.1	Organized Institutions	50.00%	Rs. 1,20,45,49,100.00
1.2	Commercial Bank	15.00%	Rs. 36,13,64,600.00
1.3	Insurance Company	15.00 %	Rs. 36,13,64,600.00
1.4	General Public	20.00%	Rs. 48,18,19,400.00

At the end of fiscal year 2010/11, NIBL has an authorized capital of Rs. 4,000 million and issued and paid-up capital is Rs. 2,409.0977 million.

(ii) Introduction to Himalayan Bank Ltd.

Himalayan Bank Ltd is the joint-venture commercial bank to be established after the restoration of multiparty democracy in the country. It was established in January 1993 with an authorized capital of Rs. 240 million. HBL was established with the joint-venture of Pakistan based bank – Habib Bank Ltd.

The head office of HBL is at Kamaldi, Kathmandu. HBL has 36 branches as per report of FY 2010/11. The policy of HBL is to extend quality and personalized service to its customers as promptly as possible. To extend more efficient services to its customers, HBL has been adopting innovative and latest banking technologies like, state-of-the-art technology and modern banking tools. HBL has access to the worldwide correspondent network of Habib Bank Limited for funds transfer, letters of credit and any banking business anywhere in the world. Besides, HBL also has correspondent arrangements with 178 internationally renowned banks like American Express Bank, Citibank and ABN Amro.

The present share capital and ownership of HBL is as follows:

1.	**Domestic Ownership**	**80.00 %**	**Rs. 1,60,00,00,000.00**
1.1	Other Entities	65.00 %	Rs. 1,30,00,00,000.00
1.2	General Public	15.00 %	Rs. 24,00,00,000.00
2.	**Foreign Ownership**	**20.00%**	**Rs. 40,00,00,000.00**
2.1	Habib Bank Ltd.	20.00 %	Rs. 40,00,00,000.00

At the end of fiscal year 2010/11, HBL has an authorized capital of Rs. 3,000 million and issued and paid-up capital is Rs. 2,000 million.

1.3 Statement of the Problem

After the liberalization policy in 1980s, the financial made some progress and prudent regulatory measure have been introduced by central bank of the country. However actual performance of the financial institution couldn't improve. Financial institution in Nepal have been facing several problems like lack of smooth functioning of economy, different policies and guidelines on Nepal Rastra Bank, political instability, security problems, poor information system, over liquidity caused by lack of good lending opportunity, increasing NPAs etc. in the present context where Nepalese commercial banks are facing the problem of increasing NPAs, more amount has to be allocated for loan loss provision. As earlier mentioned, the provision amount is taken out by deducting from the profit of the bank; the profit of the bank might come down. This research has been conducted to find out the solution of following problem:-

- What is the proportion of non performing asset in the selected commercial banks?
- What are the factors leading to accumulate of non performing asset?
- What are the guidelines and provision pertaining to loan classification and loan loss provision?
- What is the relationship between loan and loan loss provision in the selected commercial bank?

- What is the impact of loan loss provision on the profitability of the commercial banks?

1.4 Objective of the Study

The main objective of this research was to examine and analyze the non performing assets of Nepalese commercial bank. The specific objectives are:

- To examine the level of non- performing assets in selected commercial bank.
- To examine whether Nepalese commercial banks are following the NRB directives regarding loan loss provision for non performing assets or not.
- To analyze the impact of loan loss provision on the profitability of the commercial bank.
- To identify the factors leading to accumulation of non performing assets in commercial bank.
- To make recommendation tom overcome the difficulties in managing non performing assets of banks with high level of non- performing assets.

1.5 Significance of the Study

It is well known fact that the financial institution and bank in Nepal has been facing the problem of increasing non- performing assets and issue becomes more and more critical. Unfortunately nowadays banks have been becoming victims of high level of non- performing assets. Non- performing assets are those loans, which neither pay interest nor repay the principal. So, non-performing assets have been becoming subject of headache to the banking sector. Likewise Nepalese banking sectors cannot escape from such truth.

Concerning to the central library of Tribhuvan University, it has been found that there are a few research regarding non- performing assets and loan loss provision. This research will be able to deliver some of the present issues, latest information and data regarding non-performing assets and loan loss provision. Hence this study will be significant to bankers, shareholders, depositors and further researcher, students etc.

1.6 Limitation of the Study

The research is conducted to fulfill the academic requirement of Master of Business degreee. It is focused on the study of non performing asset of NIBL and HBL based of the audited financial annual reports of condition of each bank during the period 2006/07 to 2010/11. This research is tried to cover all the aspects of the non-performing assets. However the present research has the following limitation:

- This research is concerned only with the non- performing assets of commercial bank. It doesn't consider other aspects of banks.
- This research is focused on the Nepalese commercial bank and only two commercial banks have been selected as sample for the study.
- The period of the study is limited for fiscal year 2006/07 to 2010/11.
- Because of the strict policy of the commercial banks, the study is mainly based on secondary data. The data published in annual reports of respective banks, articles, publication, journal etc have been taken into consideration. Any mis-presentation, mistakes, omission etc may affect the outcome of the study. Thus, the reality of the study depends on secondary sources of the data and questionnaire filled and responses given by the respondents.
- All the analysis in this research is based on the data as of end of fiscal year i.e. end of Asadh of respective year. Any abnormality in this date may effect the conclusion of the research.

1.7 Organization of the Study

The structure of the thesis report comprises a total of five chapters which have been briefly described as follows:

Chapter 1: Introduction

To start the thesis report, this chapter includes the background of the study, introduction to NIBL, introduction to HBL, statement of problem, objective of the study, significance of the study, limitation of the study. This chapter has been targeted to help the reader to understand get the rhythm of the subject matter of the thesis report.

Chapter 2: Review of the Literature

This chapter includes conceptual review, review of relevant NRB directives and review of empirical works. For this purpose, various books, journals and periodicals as well as internet have been utilized.

Chapter 3: Research Methodology

This chapter deals with the research methodology which consist of research design, sources of dada, population and sample along with different statistical and financial tools used in this research.

Chapter 4: Presentation and Analysis of Data

This chapter illustrates the collected data into a systematic format. The analysis of these data is also included in this chapter. As well as, interpretation of analysis has also been done in this chapter.

Chapter 5: Summary, Conclusion and Recommendation

In this chapter, the summary of the entire thesis has been comprised. This chapter further describes the major findings of the thesis. Conclusions of the study have also been included in this chapter. As well as, possible and viable recommendations has also been presented in this chapter.

CHAPTER - TWO

REVIEW OF LITERATURE

The review of literature consist of examination and review some of the related books, articles published in different economic journal, bulletin, dissertation papers, magazines, newspapers and websites.

2.1 Conceptual Review

Under this heading the concept and meaning of some of the terms and the related books that are used in this study has been discussed:-

2.1.1 Loan and Advances

Loan and advances are the most profitable of all assets of the bank. This asset constitutes primary sources of income to bank. Commercial bank's main function is to create credit from its borrowed fund. The bank doing so converts liability into active asset. Loan and advances dominate the asset side of the balance sheet of any bank. They are also the least liquid form of asset of the bank. Loan and advances may take different forms and are allowed against various types of securities. Granting loan and advances always carries certain degree of risk.

Loan ad advances dominate the asset side of the balance sheet of any bank and earning from such loan and advances occupy a major space in income statement. Most of the banks failure in the world is due to shrinkage in the value of loan and advances. Hence loan is known as risky asset. Risk of non-payment of loan is known as credit or default risk.

Performing loan erodes even existing capital. If loan is given to viable project not only lenders and borrowers but also the whole society gets benefit but society losses its scarce capital if loan is given to project which is not viable.

2.1.2 Loan Classification

Loan classification refers to the process banks used to review their loan portfolio and assign loans to categorize or grades based on the perceived risk and other relevant characteristics of loan and as per guidelines of central bank. The process continues review and classification of loans enables bank to monitor the quality of their loan portfolios and take corrective action to reduce risk. In the context of Nepal, Nepal Rastra Bank has provided following directives for

classification of Loan and advances and its loss provision for the purpose of minimizing possible risk in bank's lending by using authority given by sub section 1 of section 23 of NRB Act 2012 (revised) and section 19 (ka) of Commercial Bank Act (revised). According to NRB, loan is classified into four categories:-

a) Pass loan
b) Substandard loan
c) Doubtful loan
d) Bad loan

2.1.2.1 Pass Loan

Such an asset is not a non-performing asset. In other words, it carries not more than normal risk attached to the business. This class includes the loan that principal overdue up to 3 month. It is also defined and classified as performing asset.

2.1.2.2 Substandard Loan

It is classified as non-performing asset. All loans and advances that are past due for a period of 3 months to 6 months shall be included in this category.

2.1.2.3 Doubtful Loan

All loans advances which are past due for a period of 6 months to 1 year shall be classified as doubtful loan.

2.1.2.4 Bad Loan

All loans and advances which are past due for a period of more than 1 year as well as advances have least possibility of recovery and those having thin possibility even partial recovery in future shall be classified as bad loan.

2.1.3 Performing Asset

Performing loans are those loan that repay principal and interest timely to the bank from the cash flow it generates. In the context of Nepal the loan classified as “pass” category is termed as performing loan.

2.1.4 Non Performing Asset (Loan)

Generally speaking, a, loan is classified, as non-performing loans only after it has been arrears at least 3 months. The details and classification standards of non performing loans may vary from country to country as the country put in place norm as per requirements of their own banking system. In Nepalese case the three month’s above over due rule has been adopted. It will be imperative to understand terms non performing assets (NPA) and non performing loans (NPL). Generally, non-performing assets relates to non performing financial assets. In this context, non performing assets are defined as debt instrument whose obligors are unable to discharge their liabilities as they become due. The term debt instrument refers to both loans and bonds. Therefore, non performing assets comprise the wider area of asset portfolio where as the non performing loan is referred to distressed loans classified as per regulation of central bank. Loans means loans and bills purchased and discounted by banks and financial institutions. Since the loan being the significant component on financial asset’s portfolio, non performing loans and non performing assets are used interchanging, but if there is no other asset other asset other than loans to denote, it will be better to say non performing loans. A loan is classified as non performing assets if the borrower doesn’t pay dues in the form of principal and interest for a period of 180 days past due. With a view to moving towards international best practices and to ensure greater transparency, it has been decided to adopt the '90 days overdue' norm for identification of NPAs, with effect from March 2004, default status would be given to borrower if dues are not paid for 90 days. Non Performing Asset means an asset or account of borrower, which has been classified by a bank or financial institution as sub-standard, doubtful or loss asset, in accordance with the directions or guidelines relating to asset classification issued by central bank of the country.

One should also not forget that the banks are faced with the problem of increasing liquidity in the system. Further, central Bank is increasing the liquidity in the system through various rate cuts. Banks can get rid of its excess liquidity by increasing its lending but, often shy away from such an option due to the high risk of default. The lending to the borrowers with out the proper analysis of loan proposal increases the chances of bad loan to the commercial banks.

An amount due under any credit facility is treated as "past due" when it has not been paid from the due date. Due to the improvement in the payment and settlement systems, recovery climate, up gradation of technology in the banking system, etc., it was decided to dispense with 'past due' concept.

Non-performing asset could wreck bank's profitability both through a loss of interest income and write of the principal loan amount. In the context of Nepal, loans classified as substandard, doubtful and bad are regarded as non-performing asset.

Mr. Rose defined that Non-performing assets are non income generating assets; including loans that are past due for 90 days or more change off on the other hand are loans that have been declared worthless by the banks and written off from its books. If some of these loans ultimately generate income for the banks, the amount recovered is deducted from gross change-off to yield net change off. As both of above ratios rise, the bank's exposure to credit risk grows and bank failure may be just around the corner. The final two credit risk indicators ratios reveal the extend to which a bank is preparing for loan losses by building up its loan 1005 reserve through annual charge against current income.

2.1.5 Loan Loss Provision

Loan loss provision is the fund accumulated fund that is provided as safeguard to cover possible losses upon classification of risk inherit by individual loans. There is risk inherent in every loan. Hence provisioning is made as cushion against possible losses and reflects the true picture of bank's asset. In the context of Nepal, Nepal Rastra Bank (NRB) has merely laid down the minimum provisioning requirement that should be complied with by the concerned bank on a mandatory basis. However, where there is a substantial uncertainty to recovery, higher provisioning should be made by the bank concerned. Loan loss provision is required to cover the possible harm from the non-performing loan. Loan loss provision is the accumulated fund that is provided as safeguard to cover possible losses upon classification of risk inherit by individual loans. There is risk inherent in every loan and efforts should be made to have proper control in every steps of loan management. Bank should not take risk above certain degree irrespective of return prospects. Though all the loans are at the time of disbursement, with the passes of time, they show the sign of problem. Based on the health of loan, then loan should be classified and provided accordingly provisioning is made as cushion against possible losses and to reflect the picture of showing net loan i.e. total loan minus loan loss provision in financial statements. The bank should comply with statutory regulation relating to loan classification and provisioning.

In context of Nepal, a bank requires to loan loss provision for loan advances and purchased and discounted bills as classified as per this NRB directives as follows

Table 2.1 Loan Classification

Classification of loan	Percentage of loan loss provision
Pass Loan	1 %
Sub standard Loan	25 %
Doubtful Loan	50 %
Bad Loan	100 %

(Source: www.nrb.org.np)

Loan loss provision made for performing loan is called "General Loan Loss Provision (GLLP)" and provision made for non-performing loan is called "Specific Loan Loss Provision (SLLP)".

2.1.6 Economy and NPAs

The condition of the economy and non-performing asset are reviewed briefly

(a) Nepalese Economy and NPA

Undoubtedly the world economy has slowed down, recession is at its peak, globally stock markets have tumbled and business itself is getting hard to do. The Nepalese economy has been much affected due to high fiscal deficit, poor infrastructure facilities, unstable political system, cutting of exposures to emerging markets by etc.

Further, international rating agencies like, Standard & Poor have lowered Nepal's credit rating to sub-investment grade. Such negative aspects have often outweighed positives such as increasing forex reserves and a manageable inflation rate.

Under such a situation, it goes without saying that banks are no exception and are bound to face the heat of a global downturn. One would be surprised to know that the banks and financial institutions in Nepal hold non-performing assets about 50% of total loan in government owned bank, however it is low in private sector bank. Bankers have realized that unless the level of NPAs is reduced drastically, they will find it difficult to survive.

(b) Global Developments and NPAs

The core banking business is of mobilizing the deposits and utilizing it for lending to industry. Lending business is generally encouraged because it has the effect of funds being transferred from the system to productive purposes which results into economic growth.

However lending also carries credit risk, which arises from the failure of borrower to fulfill its contractual obligations either during the course of a transaction or on a future obligation.

A question that arises is how much risk can a bank afford to take? Recent happenings in the business world – Enron, WorldCom, Xerox, Global Crossing do not give much confidence to banks. In case after case, these giant corporate became bankrupt and failed to provide investors with clearer and more complete information thereby introducing a degree of risk that many investors could neither anticipate nor welcome. The history of financial institutions also reveals the fact that the biggest banking failures were due to credit risk.

Due to this, banks are restricting their lending operations to secured avenues only with adequate collateral on which to fall back upon in a situation of default. (Source: Economic and political weekly, 2004, CARLTON PEREIRA)

(c) High Cost of Funds due to NPAs

Quite often genuine borrowers face the difficulties in raising funds from banks due to mounting NPAs. Either the bank is reluctant in providing the requisite funds to the genuine borrowers or if the funds are provided, they come at a very high cost to compensate the lender's losses caused due to high level of NPAs.

Therefore, quite often corporate prefer to raise funds through commercial papers (CPs) where the interest rate on working capital charged by banks is higher.

With the directives, banks can issue notices to the defaulters to pay up the dues and the borrowers will have to clear their dues. Once the borrower receives a notice from the concerned bank and the financial institution, the secured assets mentioned in the notice cannot be sold or transferred without the consent of the lenders.

The main purpose of this notice is to inform the borrower that either the sum due to the bank or financial institution is paid by the borrower or else the former will take action by way of taking over the possession of assets. Besides assets, banks can also takeover the management of the company. Thus the bankers will have the much needed authority to either sell the assets of the defaulting companies or change their management.

What banks should ensure is that they should move with speed and charged with momentum in disposing off the assets. This is because as uncertainty increases with the passage of time, there is all possibility that the recoverable value of asset also reduces and it cannot fetch good price. If faced with such a situation than the very purpose of getting protection would be defeated and the hope of seeing a must have growing banking sector can easily vanish. (Source: Economic and political weekly, 2004, CARLTON PEREIRA)

(d) Credit Risk and NPAs

Quite often credit risk management (CRM) is confused with managing non-performing assets (NPAs). However there is an appreciable difference between the two. NPAs are a result of past action whose effects are realized in the present i.e. they represent credit risk that has already materialized and default has already taken place.

On the other hand managing credit risk is a much more forward-looking approach and is mainly concerned with managing the quality of credit portfolio before default takes place. In other words, an attempt is made to avoid possible default by properly managing credit risk.

Considering the current global recession and unreliable information in financial statements, there is high credit risk in the banking and lending business.

To create a defense against such uncertainty, bankers are expected to develop an effective internal credit risk models for the purpose of credit risk management. (Source: Economic and political weekly, 2004, CARLTON PEREIRA)

(e) Risk in Non- Performing Loan

A realistic valuation of the financial institution's/bank's assets is essential to measure its net worth; but it is extremely difficult to get such a valuation in instances of severe corporate and financial distress, like the world economic downturn in 2001 or in a world of transition. The valuation of non-performing loans (NPL) is particularly hampered by the lack of clear market values and continuously changing economic conditions. The management of NPL and other value impaired bank assets is one of the most critical aspects of bank supervision. A widely accepted method is to hive-off the NPL of banks to a separate asset management company. Countries have taken different views on the role of asset management companies. Indonesia, Korea and Malaysia have opted for centralized public asset management companies that buy assets from private banks to help them clear their balance sheets. Thailand has aggressively liquidated the impaired assets of closed banks and financial institutions through a central agency but does not permit public sector purchases of impaired assets from private banks. They also encourage each bank to establish its own asset management company. The key to successful asset management companies is the realistic valuation of assets but it should not be a tool for the indirect bailout of existing shareholders. Sri Lanka’s banking industry too is hampered by an average of 16% NPL. To clear balance sheets of banks/financial institutions, a significant amount of public resources would be necessary which is best avoided through detailed regulatory procedures.

As evidenced in the Asian crisis a few years ago, and now in the US, the problems of banks also reflect the profound problems of the corporate sector. Hence, resolving banking problems should go hand ii hand with corporate debt restructuring. Widespread corporate insolvencies and weaknesses are much more difficult to solve and it is time consuming. The same is true for Sri Lanka’s state banks which an saddled with large public enterprise debts. The supervisory authorities alone cannot restructure banks. Bankruptcy laws, appropriate judicial systems and institutional structures are needed for this task. Until the corporate restructuring is done, there is no meaning to restructuring o insolvent banks because the complexities of the corporate would inevitably filter into banks’ books. Banking industry worldwide still believes that they are better run than in previous crises as their capital bases are stronger and their earnings are more diversified. Yet, the supervisor and regulators cannot be complacent as the aftermath corporate failures can become far more complex than one thinks.

(f) Implications of NPAs

Financial crisis emerged from Thailand in South East Asian countries largely is considered to be due to higher level of NPAs existed with the FIs. The situation was grave when the assets stopped to repay loans to credit agencies which were borrowed from overseas capital market. Investment in domestic market did not provide returns, hence the amount involved turned into non-performing while repayment schedule to lending agency overseas was matured. Failure to honors the repayment on due time was the principal reason to result in financial crisis that terminated into economic crisis in South East Asian countries. Financial crisis occurred in Asia had the higher proportion of NPAs emanate from loans which constituted highest share in the total assets of Fis. Countries with higher proportion of loan in the total assets of banks and finance companies became vulnerable while institutions with lower share of loans in the total assets were affected less. Of the total assets of commercial banks in Nepal, total credit accounted 47.2% in the fiscal year 1997/98 (NRB, 1999). Similarly India had the proportion of loan in the total assets as 42.0% while those figures for Thailand, Indonesia and Malaysia were 78%, 70%, and 69 percent respectively (Mukherjee, 1998).

Empirically, it has been seen that Nepal and India having lower proportion of loan in respect of total assets provided cushion to make ample provision and therefore were least affected by the financial crisis. On the other hand the South East Asian with relatively higher proportion of loans in the total assets of the victim of the shock of regional crisis.

The credit institutions are repelled from further investment after the interest accrual or due principal repayment has stopped. Interest incomes from such assets are reduced to the extent of declared amount as NPAs. As the assets declared NPA emanate from the deposits, it puts the depositors fund at risk. The credit agencies are put to an extra amount of liability by regulatory authorities in the form of provision. The amount required for provision depends on the level of NPAs and their quality. Rising level of NPAs create a psyche of worse environment especially in the financial sector. Depositors are not interested to save. Rather the hard earned savings are diverted to consumptions. Consequently the savings pattern hence investment is affected thereby creating an unhealthy atmosphere in the financial sector.

2.2 Review of Relevant NRB Directives

Nepal Rastra Bank has issued guidelines on provisioning requirement with respect to bank advances. Among various directives issued in 2001 directive number 2 is relating to loan classification and provisioning. Effective from fiscal year 2058/59 (2001/02), banks have classified outstanding loan and advances on the basis of aging of principal into following four categories:-

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

(b) **Substandard Loan:** Loans/advances which are overdue by a period from three months to a maximum period of six months.

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

(d) **Loss/Bad Loan:** Loans/advances which are overdue by a period of more than one year. It is also called bad loan.

The loans which are in pass class and which have been rescheduled/restructured are called as the performing loan, and the sub-standard, doubtful and loss categories are called non-performing loans.

In terms of NRB guidelines, as and when an asset becomes a NPA, such advances would be first classified as a sub-standard one for a period that should not exceed 6 month and subsequently as doubtful assets.

It should be noted that the above classification is only for the purpose of computing the amount of provision that should be made with respect to bank advances and certainly not for the purpose of presentation of advances in the bank's balance sheet. The directives of NRB relating to classification and provisioning of loan and advances are changing over time. Here is the table which shows the loan classification of last four years.

Table 2.2 Time Table of Loan Classification

Classification	Pass Loan	Substandard Loan	Doubtful Loan	Bad Loan
For FY 2001/02	Loans not past due and past due up to 3 month.	Loans and advances past due for a period of over 3 months to 1 year	Loans and advances past due for a period of over 1 year to 3 year.	Loans and advances past due for a period of over 3 year.
For FY 2002/03	Loans not past due and past due up to 3 month.	Loans and advances past due for a period of over 3 months to 1 year	Loans and advances past due for a period of over 1 year to 3 year.	Loans and advances past due for a period of over 3 year.
For FY 2003/04	Loans not past due and past due up to 3 month.	Loans and advances past due for a period of over 3 months to 9 months.	Loans and advances past due for a period of over 9 months to 2 year.	Loans and advances past due for a period of over 2 year.
For FY 2004/05	Loans not past due and past due up to 3 month.	Loans and advances past due for a period of over 3 months to 6 months	Loans and advances past due for a period of over 6 months to 1 year	Loans and advances past due for a period of over 1 year.

(Source: www.nrb.org.np)

2.2.1 Additional Arrangement in Respect of "Pass Loan"

Loans and advances fully secured by gold, silver, fixed deposit receipts and HMG securities shall be included under pass category. However, where collateral of deposit receipts or HMG securities or NRB bonds is placed as securities against loan for other purposes, such loan has to be classified on the basis of ageing. (Source: www.nrb.org.np)

2.2.2 Additional Arrangement in Respects of "Loss Loan"

Even if the loan is not past due, loan having any or all of the following discrepancies shall be classified as "loss" (Source: www.nrb.org.np)

1. The borrower has declared bankrupt.
2. No security at all or security that is not in accordance with the borrower's agreement with bank.
3. The credit has not been used for the purpose original indented.
4. Loans provided to the borrowers included in the backlist and where the credit information bureau blacklist the borrower.
5. Purchased or discounted bills are not realized within 90 days from the due date.
6. The borrower is absconding or cannot be found.

2.2.3 Loan Loss Provision

As and when an asset is classified as an NPA, the bank has to further sub-classify it into sub-standard, doubtful and bad assets. Based on this classification, bank makes the necessary provision against these assets. Nepal Rastra Bank has issued guidelines on provisioning requirements of bank advances where the recovery is doubtful. Banks are also required to comply with such guidelines in making adequate provision to the satisfaction of its auditors before declaring any dividends on its shares.

In case of a sub-standard loan, a general provision of 25% of total outstanding should be made.

In case of doubtful loan, guidelines requires the bank concerned to provide entirely the unsecured portion and in case of secured portion an additional provision of 50% of the secured portion should be made depending upon the period for which the advance has been considered as doubtful.

In case of bad loan, guidelines specifically require that full provision for the amount outstanding should be made by the concerned bank. This is justified on the grounds that such an asset is considered uncollectible and cannot be classified as bankable asset.

The summary of provision that a bank is required to loan provision for loan advances and purchased and discounted bill has classified as per this NRB directive follows:-

Table 2.3 Loan Classification and Loan Loss Provision

Classification of loan	**Period of overdue**	**Loan loss provision**
Pass Loan	Not overdue and overdue up to 3 months	1%
Sub-standard	Overdue loan from 3 months to 6 months period	25%
Doubtful Loan	6 to 12 month overdue loans	50%
Loss Loan	More than 1 year period overdue loans	100%

Loan loss provision made for performing loan is called “General Loan Loss Provision” and provision made for non-performing loan is called “Specific Loan Loss Provision”. (Source: Unified Directives of Nepal Rastra Bank)

2.2.4 Additional Provisioning in the Case of Personal Guarantee Loans

Where the loan is extended only against personal guarantee, a statement of assets and equivalent to the personal guarantee amount not claimable by any other shall be obtained. Such loan shall be classified as per above and where then loans fall under the category of pass, substandard and doubtful loan in addition to the normal loan loss provision applicable for category , an additional provision by 20 percentage point shall be provided. Classification of such loan and advances shall be prepared separately. Hence the loan loss provision required against the personal guarantee loan will be 21%, 45% and 70% for pass, substandard and doubtful category respectively. (Source: Unified Directives of Nepal Rastra Bank)

2.2.5 Rescheduling and Restructuring of Loan

In respect of loan and advances falling under the category of substandard, doubtful or loss, bank may reschedule or restructure such loans only upon receipts of a written plan of action from the borrower citing the following reason:- ((Source: Unified Directives of Nepal Rastra Bank)

(a) The reduced degree of risk inherent to the borrower determined by analyzing its balance sheet and profit and loss account in order to estimates recent cash flows and to project future ones, in addition to estimates recent cash flows and to project future ones. In addition to assessing market condition.

(b) The internal and external causes contributing to detritions of the quality of loan.

(c) An evaluation of the borrower's management with particular emphasis on efficiency, commitment and high standards of business ethics.

(d) Evidence of existence of adequate loan documentation.

2.2.6 Loan Loss Provisioning on Respect of Rescheduled, Restructured or Swapped Loan

(a) Except for priority sector, in respects of all types of reschedule or restructured or swapped loan, if such credit falls under pass category according to NRB directives, loan loss provisioning shall be provided at minimum 12.5%.

(b) In case of rescheduling or restructuring or swapping of insured or guaranteed priority sector credit, the loan loss provisioning shall be provided at one fourth of the percentage mentioned in clause (a).

(c) In respect of swapped loans, the bank accepting the loans in swapping has tom provide loan loss provision classifying the loan under the same classification as were existing. The bank accepting the loan in swapping shall obtain certification from the concerned bank of financial institution as to the existing classification.

(Source: Unified Directives of Nepal Rastra Bank)

2.2.7 Provision against Priority Sector Credit

Full provisioning as per normal loan loss provisioning shall be made against three uninsured priority sector and deprived sector loans. However in respect of insured loans the requisite provisioning shall be 25% of the percentage of normal loan loss provisioning. The required provisioning in the case of insured priority/deprived sector credit is as follows:

Table 2.4 Loan Classification of Priority Sector

Loan	Percentage of Provision
Pass	0.25%
Substandard	5%
Doubtful	12.5%
Bad	25%

In case of rescheduling, restructuring or swapping of insured or guaranteed priority sector, the proportion of loan loss provision would be 3.125% i.e. 25% of 12.5%. (Source: Unified Directives of Nepal Rastra Bank)

2.3 Review of Relevant Articles

Different articles relating to the non-performing asset is reviewed here.

Dhungana (2004) explains that Asset Management Company (AMC) for resolving the problem of non-performing loan (NPL). According to Mr. Dhungana, AMC is the specialized financial institutions who buy the NPL from financial institution and take necessary steps to recover the maximum value from the acquired assets. As per his view, NPL are not resolved in time there would be inherent direct cost to the economy. As stated by him NPL may rise due to the external factors like decreases in market value of collateral, deterioration in borrower's repayment capacity, economic slowdown, borrower's misconduct, improper credit appraisal system, lack of risk management practice, ineffective credit monitoring and supervision system. Hence he suggested that, NPL should be kept at minimum level and the specialized institution such as AMCs should manage the distressed loans.

He says that, both traditional and AMC are available to deal with NPL problem. Under traditional approach, bank handless the NPL's in its own way especially through recovery unit who focus on continuing negotiation with the borrower and give top priority to the loan recovery. As per him, this approach is useful in dealing with small business loans where personal touch is adopted but for big loans this approach does not work. AMC seems as the only realistic option when the financial sector recovery is the underlying objective in financial system where the institution fails to resolve the NPL problem through their own effort. He stated that the main advantage of establishing AMC is that AMC is able to move in an expeditious manner removing the distraction of managing NPLs from the banking system and frees up resources within the financial institutions allowing them to concentrate on their core activities.

He concludes that as in most of the countries, Nepalese financial system is largely dominated by the banking sector. The banking sector is severely affected by the NPL problem, it is estimated the NPL of the Nepalese Banking system is around 16%. Therefore there is no doubt that it has serious implication on the economic performance of the country. It will be the eclipse\e in the development of financial soundness in the economy, if not controlled in time. However, traditional or AMC rot can be practiced to get recovery from this sickness of the financial system, the AMC root may be more effective approach to be quick recovery as it has been experienced around the world.

Neupane (2003) described some views regarding bad loans of banking sector. As mentioned by him there was various types of risk inherent in the credit. One, who manages risk, earns profit. He further added that the recent financial crisis in banking sector is due to weak accounting procedures, defect on loan classification, lack of transparency, loss control measures etc.

Neupane (2003) has also stated that NPL is the indicator of financial crisis and the factor leading to NPL is economic slowdown, recession, bad intention of borrower, lack of credit policy, and increase in interest rates. NPL increases resource mobilization cost and reduce profit earning capacity of the bank. He has also mentioned that the international standard of acceptable NPA is 4% but there is about 26% NPA in Nepalese banking sector which is due to the high level of NPL of two nationalized banks. As stated by him, the major implication of NPL is banks can’t return depositors money on demand and it limits lending capacity of the bank. The writer has suggested internal and external measure for reducing NPL and its effect. Internal measure comprises classification of loans and advances and providing provision for probable loss and external measures comprises of help from Credit Information Bureau (CIB), appointment of Asset Management Company (AMC) and Debt Recovery Tribunal (DRT).

He concludes that bank must give priority for reducing NPA. He has also mention that many countries are adopting various measures for reducing loan loss. Recently the president of Philippines has announced tax rebate system for reducing NPA. Now it is high time to improve bad debts of banking sector with firm determination.

Sapkota (2001) explains that the main purpose of establishment of bank in to collect idle fund general publics disburses them to needy people /institution in the form of loan and advances. Loan and advances are given for a certain period of time but it is not sure that all the loans are recovered within time. Then function of any commercial bank is recovered easily within stipulated time. Hence is often said that, it is easy to disburse loans but as much hard to recover loans and interest.

He stated that as per new provision, loans and advances are classified on the basis of ageing of past dues and collateral value. On that basis loans and advances need to be classifying into four categories namely pass, substandard, doubtful and loss. With the change in time and demand, change was made in provision of loan classification and provisioning. He has also mentioned that previously loans and advances are categorized into six categories as pass, acceptable, indicative substandard, substandard, doubtful and loss. With the old provision the loan would be non-performing only if it is past due for that 1 year but as per new provision, the loan would be non-performing if the loan is past due for more than three months.

He concludes that these changed provisions would contribute to healthy, transparent and inherent risk bearing capacity of the banks. If NPL increases it affects adversely to the various sectors. Hence the writer concluded with the hope that new provision if properly implemented would help to reduce NPL and helps banks from financial crisis.

Chawala (2000) explains that about the non performing asset and its impact. “Any lending involves the following three stages where discretion needs to be exercised (a) Evaluation and assessment of the proposal (b) Continuing Support during the currency of the loan by additional loan or by non-fund based activities (c) Exit decision and modality. A rule-based approach precludes reasonable application of mind. Evaluation of project idea and the management is something that most banks are least equipped for. This leads to the banker acting too liberal on all projects that are related to the flavor-of-the-month as well as to insisting on collaterals from everyone without taking into consideration any other competencies of the entrepreneur. Banks are too willing to finance against such reports to shady businessmen who may also sometimes grease their palms instead of looking for genuine project ideas backed by competent men of integrity. Herd mentality of the bankers creates excess capacity in any industry that they choose to finance thereby laying the seeds of sickness of that industry. Coupled with the in competency of the entrepreneurs and the shady intentions with which the projects were set up, the sickness spreads like wild fire. After a loan has been disbursed, it is an accepted norm that the Bank has a duty to keep smelling for and to act promptly on key signals that indicate the health of the recipient of the loan. Rule-bound bankers do collect all the necessary information and pile it up in neat reports and files. It is not unusual for bankers to even advise their clients to cook up their accounts to either satisfy the Banker's Health Code requirements or to get their unit classified as sick under the relevant laws. This having been done, the banker can sleep peacefully. Acting on the signals that emanate from these reports is none of his business. It is the entrepreneur who has to exercise to convince a long chain of stubborn bank officers to rise from their slumber. The entrepreneur is now caught in a game where almost every petty Bank officer satisfies his ego by kicking him where it hurts most before obliging him by moving the file to the next officer. Banks key decisions about nursing versus exit get influenced by this merry-go-round ego trip of the officers. The attitude that the bank will lose more than the entrepreneur by a delay in such key decisions is completely missing who see themselves.

India Infoline Limited explains that fundamentally Credit Rating implies evaluating the creditworthiness of a borrower by an independent rating agency. Here objective is to evaluate the probability of default. As such, credit rating does not predict loss but it predicts the likelihood of payment problems.

Credit rating has been explained by Moody's a credit rating agency as forming an opinion of the future ability, legal obligation and willingness of a bond issuer or obligor to make full and timely payments on principal and interest due to the investors.

Banks do rely on credit rating agencies to measure credit risk and assign a probability of default.

Credit rating agencies generally slot companies into risk buckets that indicate company's credit risk and is also reviewed periodically. Associated with each risk bucket is the probability of default that is derived from historical observations of default behavior in each risk bucket.

However, credit rating is not fool-proof. In fact, Enron was rated investment grade till as late as a month prior to it's filing for Chapter 11 bankruptcy when it was assigned an in-default status by the rating agencies. It depends on the information available to the credit rating agency. Besides, there may be conflict of interest which a credit rating agency may not be able to resolve in the interest of investors and lenders.

Stock prices are an important (but not the sole) indicator of the credit risk involved. Stock prices are much more forward looking in assessing the creditworthiness of a business enterprise. Historical data proves that stock prices of companies such as Enron and WorldCom had started showing a falling trend many months prior to it being downgraded by credit rating agencies.

The Boss - KFA (2007) researches that made on analysis of non performing loan of Nepalese financial sector to feature the loan position of Nepalese financial sector. It is said that the banking sector mirrors the larger economy. It’s linkage to all sectors makes it a proxy for what is happening in the economy as whole. Indeed, the Nepalese banking sector today is at boiling point. The financial sector has evolved as the biggest sector in the economy. There are altogether 128 financial institutions in the country and currently more than 20000 people employed in these financials institution. These people is responsible for managing approximately NPR 221 billion worth of assets (primarily loans and advances), out of which 50 percent comprises of two large banks- Rastriya Baninjya Bank and Nepal Bank Limited. Annual net profit of 5.89 billion generated by creating asset worth of NPR 221 billion last year means a very low return on asset (more 2.1 percent), which is even below the average savings deposit rate in the country.

While doing root cause analysis for this scenario, two very strong reasons have evolved. The first reason is the poor quality of loans, more particularly in government-owned banks and some private banks, due to non compliances of basic credit principles while granting loans coupled with lack of credit skills assessment. The second reason for lower return can be attributed to the fact that almost all the financial institutions are involved only in dealing with undifferentiated vanilla banking products. An interesting example in this regard would, if someone needs a car loan, which is typically a commercial bank product, he or she can walk into any development bank in the country. Yes, in the current scenario, it is very difficult for development banks in the country to burn their fingers by going into long-term project loans. However, they should be able to create their own niche market.

In order to create a niche market, product-specialization is a must and the banking sector is way below average in terms of introducing and implementing value-added banking products in the areas of trade finance, credit, remittance and more importantly in global market areas.

Loan is the most critical factor in determining the strength of any bank. Primary factors that can be considered are the quality of loan portfolio, mix of risk assets and credit administration system.

Loan NPL ratio indicates the better risk assessment and robust credit management systems in place and vice versa. At the same time, while higher loan loss provisions indicates poor credit management, it also indicates adequate reserve for possible loan loss and protects the balance sheets of respective banks.

In a period of three years (from 2002/03 to 2005/06), total loans and advances of commercial banks has increased by 46 percent. When we consider this period, we know that this phase has been hit by situations like political uncertainly, conflict and unrest in the country. Even in this kind of scenario, the overall banking sector has been able to increase its asset base by significant percentage indicates that they have been capable in switching their areas of investments.

Ghimire (2003) exp1ains that tried to highlight the effects of change or amendment in NRB directives regarding loan classification and loan loss provisioning. “Although the circumstances leading to financial problem or crisis in many Nepali banks differ in many respects, what is common across most of the banks is the increased size of non performing assets (NPAs). To resolve the problem of the losses or likely losses of this nature facing the industry, NRB has, as the central bank, amended several old directives and issued many new circulars in the recent years.

As opinioned by him, since majority of the commercial banks of the country as present falls under substandard, doubtful and even loss categories, loan loss provisioning now compare to previous arrangement would be dramatically higher. The new classification and provisioning norms are very lent able as they help to strengthen banks financially. He added that we also must remember that the old system remained in force from 1991 to 2001, which was probably the most volatile decade of the business operation of the country. He has indicated that Loan Loss Provisioning as a percentage of total credit of April 12, 2001 is 5.2% but as April 13, 2003 it has jumped to 18.39%. If only private banks are considered, it is 2.12% of April 2001 where as it is 6.30% as of April 13, 2003. The total increment in LLP is Rs 11,328.11 million and the total increment in credit is only Rs 7,976.70. He has also stated that tightening provisioning requirements on NPL is essential to ensures that banks remain liquid even during economic downturns.

In the conclusion he has mentioned that in the recent years NRB has worked for management and reform of the credit of the financial institution more seriously and NRB has adopted reforms aimed not just as dealing with problem banks but also at strengthen banking supervision to reduce the likelihood of future crisis. “All prudential directives of NRB in connection of credit sector reform have been made revised on April 2001. To adopt such changes there can be some difficulties and for a better and harmonized reform NRB should continue to be supportive, proactive and also participative to take opinion of bankers for a change in regulation, policy taking place in future.

Tiwari (2004) explains that Nepal‘s financial sector is moving like a ‘sinking boat’. As per his view financial institution have failed in delivering beneficial services to needy people by developing growth is credit-giving centers in rural areas without which sustained economic growth is impossible. On the other hand banks and financial institutions have enough liquidity but they are finding it difficult to find suitable places for investment.

“Problems such as insecurity lack of market research from banks, low investment opportunities, weak operational policies for carrying out financial transaction, among others have contributed to the problems of this sector. Despite central bank’s directives regulating banks and financial institution, private and government banks are functioning haphazardly. Nepal Bank Limited (NBL) and Rastriya Banijya Bank (RBB), the two largest banks, occupy about 50 percent of the country’s banking assets. Effective reform of these two is key to improved performance of the whole sector. The process currently underway to reform these two institutions, despite paying huge amounts to foreign experts, has not given expected results. ….. Besides NBL and RBB, the Non Performing Assets (NPA) of some private banks also very high. If the government and central bank allow the financial sector reforms to focus only on RBB and NBL, it might become a futile effort. The current management of RBB and NBL has not able to reduce their NPL even after two years, which have crossed over 60 %. Earlier KPMG had calculated NPL at 30-35 percent. The central bank itself says, despite efforts NBL has high NPL s and negative capital of Rs 9.75 billion.

The writer suggested that the forthcoming budget should not remain a document merely but should address financial sectors ills with a wide vision. He further recommended that in order to create a well regulated, prudent, market oriented, competitive and strong financial system in Nepal, the government should look to build upon its indigenous strength and improve upon its regional ties to improve its efficiencies.

Dhungana (2006) explains that the position of the non-performing loan and causes that results the non performing loan in Nepalese banking system. Extension of credit is one of the major activities of banks and financial institution. Credit usually represents the bulk of the institution's earning assets. Interest on credits is major source of income and profitability for the banks and financial institution. Therefore, quality credit management is a subject of crucial importance in the bank and financial institutions to maintain sustainability and improving operational efficiency. Poor credit management and deterioration in the quality of loans give birth to NPLs. The internal measures play significant role to control the growth of NPLs. Best credit practices, culture and policies are required to strengthen the internal factors. The banks should have a proper system and competency on risk management and should insure that risk is accurately identified, assessed and controlled property. A proper risk management is undoubtedly an important tool for a good banking and NPL's management.

The problem of non-performing loan has been the major issue on banking sector reforms agenda. Nepal Rastra Bank is very much concerned with this issue and initiating various measures to enhance the risk management capacities, introducing policies and issuing regulations in this regard. However, the level of NPL's in the banking system is decreasing with the implementation of comprehensive financial sector reform program, but it is still at astounding level at around 18 percent at mid July 2005. The level of NPL in the financial system of Nepal comprising of 17 commercial banks, 25 development banks, 9 micro credit development banks and 60 finance companies is around 17 percent (Rs 29.0 billion) as at July 2005. Unless and until the problem of NPL is resolved, the growth and stability of the financial system can not be assured. Therefore, the problem should be resolved as soon as possible. In order to resolve the problem, preventive and curative measures are required to be initiated in the system. Preparation of best CPG, establishing best credit approval of the preventive measures to control the NPL's growth. Curative measures such as assisting the banks and financial institutions to dispose the distress loans and facilitating to recover NPLs are also equally important when the NPL's are already at astounding level. However, various preventive and curative measure have been initiated within current comprehensive financial sector reform program but we still have to go through a long journey in strengthening both the internal factors and external factors in order to lower down the existing level of NPL's and to create such a environment where NPL's could be maintained at the tolerable limits. Therefore, both strengthening of the internal capacity of the financial institutions and improving capacity of the system as a whole is the need of the day. It can be expected that the financial sector reforms will have very positive impact in lowering down the level of NPL from the existing level and strengthening the internal capabilities of the banks and financial institutions in order to manage the credit portfolio efficiently and effectively in the days to come.

2.4 Review of Relevant Thesis

Shrestha (2004) has tried to find out the impact of the non performing loan on commercial banks. She also tried to find out the impact of NRB directives on Commercial banks. She has also made effort to find out whether the directives are actually followed by the three selected banks for the research. As per her view the process of continual review and classification of loan and advances enable banks to monitor the quality of their loan portfolios and to take then remedial action to counter deterioration in the credit quality of their loan portfolios.

She concluded that with the new provision guided by the NRB, the banks will have its provision amount increasing on coming years and subsequently profitability of the banks will also come down. However the true picture of the quality of these assets will be cleared in the coming years to come. She recommends, "The banks should be very careful while analyzing the paying capacity of its credit clients. With longer period of past due, the bank will end up increasing its provision which will keep the bottom line low if bank is not careful**".**

Pandey (2002) has tried to find out the impact of changes in NRB directives on the performanc4e of the commercial banks and also find out whether the directives were implemented or not. The directives if not properly addressed have potential to wreck the financial system of the country as they are only tool of the NRB to supervise and monitor the financial institutions. The directives in themselves are not that important unless properly implemented. The implementation part depends on the commercial banks. In case of commercial banks are making such huge profit with full compliance of NRB directives, then the commercial banks would votes of praise because they would then be instrumental in the economic development of the country. All the changes in NRB directives made impacts on the bank and the result are the followings:-

(a) Ratios and more stringent loan related document.

(b) Increase in A short term decrease in profitability which result to lesser dividends to shareholders and lesser bonus to employees.

(c) Increase protection to money of the depositors through increased capital adequacy operational procedures of the bank which increases the operational cost of the bank.

(d) Reduction in the loan exposure of the bank, which decreases the interest income but increases the protection of depositor’s money.

All the aforesaid results lead to one direction, the bank will be financial healthy and stronger in the future.

HBL will be able to withstand tougher economic situation in the future with adequate capital and provision for losses. The tough time through which bank is undergoing at present will prevail only for a couple of years but in the long run, it will be strong enough to attract more deposits and expose itself to more risk with capital cushion behind it. The quality of the assets of the banks will become better as banks will be careful before creating credit. Ultimately, the changes in the directives will bring prosperity not only to the shareholders but also to the depositors, the employees and the economy of the country as a whole.

Pandey (2002) recommends that the bank has to make its monitoring and follow up department stronger to give priority in human resource development through training to its staffs and make them efficient enough to monitor and collect already disbursed loans.

Khadka (2004) has tried to find the impact of non-performing assets and loan loss provision on financial position of the banks. Non-performing assets are non income generating assets, including loans that are past due for 90 days. Non-performing asset could wreck bank's profitability both through a loss of interest income and write of the principal loan amount. The loans are classified according to NRB directives into pass, substandard, doubtful and bad loan. Based on this classification, bank makes the necessary provision against these assets. Nepal Rastra Bank has issued guidelines on provisioning requirements of bank advances where the recovery is doubtful. Banks are also required to comply with such guidelines in making adequate provision to the satisfaction of its auditors before declaring any dividends on its shares.

The commercial banks must pay attention on loan granting to their customers. This can be done through the loan approval process. The bank must utilize depositor's money as loan and advances to get success in competitive environment. The largest part of the bank in asset side is loans and advances. He concluded that any negligence in administrating loan and advances could be the main cause of a liquidity crisis in the bank and one of the main reasons of a bank failure.

Ojha (2002) has tried to carry out the research is to analyze the various aspects of bank's lending in various productive and priority sector, the individual bank's performance regarding the lending quantity, quality, efficiency and its contribution in total income.

As stated by him, over liquidity caused due to lack of good lending opportunities, risk arising due to mismanagement of lending portfolio, increasing non-performing loan etc are some of the problems that is facing by the Nepalese banking sector.

Ojha (2002) conclude that the highest growth rate, proportionately high volume of loans and advances, the best contribution in agriculture and priority sector and the level of deposit mobilization of HBL has put this bank in top position in the lending function. However the better activity ratio of Standard Chartered Bank has proved this bank is the best in managing the lending portfolio according to the demand of profit oriented organization. The high volume of lending activities and high level of productive sector loan of Nabil has put the bank in the top position in absolute terms. The increasing loan loss provision and high volume of non performing loan of HBL and Nabil is the serious matter. The high volume of the NPA of HBL may have caused due to the failure of industrial and agriculture sectors. Nabil's increased NPA may have caused due to the accumulated bad debts that is kept behind the curtain to show the high efficiency of management. As per his opinion, lack of proper credit appraisal, default by blacklisted borrower and professional defaulter, over confidence in commercial banks regarding credit appraisal efficiency and negligence in taking the credit information relating to borrowers etc has caused many of bad debts in these banks.

By conducting the research work on lending practices, he is enabling to suggest the following suggestion to the financial sectors.

(a) Financial sectors (banks in this study) should be more cautious and realistic while granting loans and advances.

(b) To reduce the risk of high NPA, the banks should avoid lending in more risk area until the bank doesn't fully satisfy itself regarding the future viability of Asset Management Company which helps commercial banks in collecting their debts and improving their credit rating efficiency.

(c) To lower the level of NPA, the commercial banks should take necessary information from the Credit Information Bureau.

(d) Commercial banks should be utilized it deposits in to productive sectors of the economy. However the commercial banks should not neglect the priority sectors to lend.

Shrestha (2003) has tried to find out the impact of NRB directives on commercial banks. She has also made effort to find out whether the directives are actually implemented and are being monitored by NRB or not. She has stated that both Nabil Bank Ltd. and Nepal SBI Bank Ltd. are implementing the NRB directives.

Shrestha (2003) concludes that all the changes in NRB directives made both positive and negative impacts on the commercial banks. Even this study is limited to only two samples i.e. Nabil bank and Nepal SBI Bank, among entire population, it clears the new directives issued by NRB make good impact more than bad impact on the various aspects of the banks. It can be seen that the provision has been changed and the increased provisioning amount has decreased the profitability of commercial banks. Apart from, loan exposure has been cut down to customers due ton the borrower limits have been brought down by NRB. Therefore reduction in loan amount results to decrease the interest income from loans, which will decrease the profits of the banks in coming years. Decreasing profitability push towards lesser dividends to shareholders and lesser bonus to employees. Not only the negative side but also there positive side of new directives. Recently the problems of banks are increasing operating cost and decreasing loan amount resulting decrease in the profit of the banks. But it shows it is only for short term because the directives are more effective to protect the banks from bad loans, which protect the banks from bankruptcy as well as protection of deposits of depositors. Increase in capital adequacy ratio strengthens; the bank's financial position, loan related provision will make safety of loans except the risk reducing provisions will protect the bank from liquidation. Above all, it can be concluded that newly issued directives are more effective than previous in although it has brought some problems towards banks. To decrease the decreasing profits of the banks, they should research the alternatives such like more investments in other business; bank should adopt new technology according to the demand of time and depend on only interest income for profits.

Khadka (2002) has found out the relationship between deposits, investments, loans and net profit. She has made the following conclusion while comparing the performance of NBL with Nabil, SCBNL and NIBL.

Khadka (2002) concludes that NBL is comparatively less successfully in on balance sheet as well as of balance sheet operations than that of other CBs. It predicts that in the coming days if it could not mobilize and utilize its resources as efficiently as other CBs to maximize the returns, it would bag behind in the competitive market of banking. A profitability position of NBL is comparatively worse than that of other CBs. It predicts that NBL may not maintain the confidence of shareholders, depositors and its all customers if it cannot increase its volume even in future.

As the bank experience many difficulties in recovering the loans and advances and their large amount is being blocked as non performing assets, she suggested that there is an urgent to workout a suitable mechanism through which the overdue loan can be realized.

Shilpakar (2003) aimed to analyze performance of finance company regarding lending quantity and quality and its contribution in profitability. She concluded that loans and advances is one of the main sources of income of finance companies. This is what is also shown by the high degree positive correlation between total income and also loans and advances. “Loan loss provision is like a by product of loans and advances increase in synchronize.

2.5 Research Gap

By the study of various research and articles, it has been found that increasing non-performing asset followed by increased loan loss provision is one of the challenges faced by commercial banks in the present context. Some research were done in which matter relating to loan loss provisioning has been discussed but no research was found in detailed analysis of non-performing loan and loan loss provisioning. Hence this research has attempted to fill this research gap by taking reference of Nepal Investment Bank Limited and Himalayan Bank Limited. This research will be able to deliver some of the present issues, latest information and data regarding loan classification and loan loss provisioning.

After reviewing the relevant literatures, the next chapter concentrates in research methodology applied in the research.

CHAPTER - THREE

RESEARCH METHODOLOGY

Research methodology is the method to solve the research problem systematically. It may regard as a science of studying how research is done to conduct the research. It is very important to conduct the research. In research methodology various sequential steps that are generally adapted by the researcher, studying his research problem among with certain objectives in view are studied. Research methodology helps us to find out accuracy, validity and suitability. Research is a systematic inquiry of any particular topic and the methodology is a method of doing research n a well manner. Hence research methodology is the systematic study of research problem that solves them with some logical evidence. The research methodology adopted in present study as discussed below:-

3.1 Research Design

Research design is the plan, structure and strategy of investigation conceived so as to obtain to research question and control variances. The plan is the overall scheme or programmed of a research. This research is aimed at studying the non-performing asset and loan loss provisioning of commercial bank. For this purpose, this research will follow analytical and descriptive design.

3.2 Population and Sample

Population refers to the entire group people, events or things of interest that a researcher wishes to investigate. Since this study is about non-performing asset and loan loss provisioning of commercial bank, the population for this study comprised all the licensed commercial banks of the country.

A total of 32 commercial banks were licensed to operate. The commercial banks of Nepal are categorized into private and public sector bank. The public sector banks include Nepal Bank Limited and Rastriya Banijya Bank and private sector bank comprise remaining banks. Out of them two commercial bank is selected for this research. They are

- Nepal Investment Bank Limited
- Himalayan Bank Limited

3.3 Sources of Data

The data used in this research is primary and secondary. The sources of primary data are bank employees of concerned organization while following are the sources of the secondary data:-

- Annual reports, newsletter, broachers etc. of concerned banks.
- Laws, guidelines and directives regarding the subject matter.
- Text books
- Article published in newspaper, journal, magazine and other publication.
- Various reports published by NRB, CIB, NIBL, HBL etc.
- Various related websites

3.4 Data Collection Techniques

The technique used to obtain the primary data is questionnaire, direct interview, and field visit and telephone inquiries. The annual reports of Nepal Investment Bank Limited and Himalayan Bank Limited were from the concerned banks and other reports were downloaded from the websites. Various publication of NRB was collected from concerned department of NRB Baluwatar. Similarly reports of Credit Information Bureau (CIB) have been collected from office of CIB, Thapathali. The references of NRB directives and guidelines have been obtained from NRB Office and websites of NRB. Various reports, textbooks, journal and unpublished dissertation have been obtained by visiting Tribhuwan University central library, Shankerdev Campus Library.

3.5 Data Analysis Tools

The data collected from different sources are recorded systematically and identified. The available information is grouped as per the need of the research work in order to meet research objectives. The collected data are presented in appropriate forms of table and charts. For analysis purpose different kind of appropriate mathematical, statistical and financial tools have been applied. Furthers represent the data in simple form diagrams and graphs have also been used.

3.5.1 Financial Tools

While adopting financial tools, a ratio is used as benchmark for evaluating the financial position and performance of any firm. "Financial analysis is the process of identifying the financial strength and weakness of the firm by properly establishing relationship between the items of the balance sheet and profit and loss account." Financial analysis is the use of financial statements to analyze a company's financial position and to assess future financial performance.

3.5.1.1 Ratio analysis

Ratio analysis is widely used tool of financial analysis. A ratio is simply one number expressed in terms of another and as such it express the numerical or quantitative relationship between two variables. Ratio analysis reflects the relative strength and weakness of any organization and also indicates the operating and financial growth of the organization. "Ratios help to summarize large quantities of financial data and to make quantitative judgment about the firm's financial performance. The relationship between two accounting figures expressed mathematically is known as financial ratio". Even though there are many ratios, only those ratios has been calculated which are related to the subject matter.

Following ratios have been computed and analyzed in this study.

(a) Loans and Advances to Total Asset Ratio

Loans and advances of any commercial banks represent the major portion in volume of total assets. The ratio of loans and advances to total assets measures the volume of loans and advances in the structure of total assets. The high degree of ratio indicates the good performance of the banks in mobilizing its fund by way of lending functions. However in its reverse side, the high degree is representative of low liquidity ratio. Granting loans and advances always carries a certain degree of risk. Thus this asset of banking business is regarded as risky assets. Hence this ratio measures the management attitude towards as risky assets. The low ratio is indicative of low productivity and high degree of safety in liquidity and vice versa. This ratio is calculated as follows:

$$\text{Loan and Advances to Total Asset Ratio} = \frac{\text{Loans and Advances}}{\text{Total Asset}}$$

(b) Loans and Advances to Total Deposit Ratio (CD Ratio)

The core banking function is to mobilize the funds obtained from the depositors to borrowers and earn profit and CD ratio is the fundamental parameter to ascertain fund deployment efficiency of commercial bank. In other words this ratio is calculated to find out h9ow successfully the banks are utilizing their total deposits on credit or loans and advances for profit generating purpose as loans and advances yield high rate of return. Greater CD ratio implies the better utilization of total deposits and better earning, however, liquidity requirements also needs due consideration. Hence 70%-80% CD ratio is considered as appropriate. This ratio is calculated by dividing total credit by total deposit of the bank.

$$\text{Loan and Advances to Total Deposit Ratio} = \frac{\text{Loans and Advances}}{\text{Total Deposit}}$$

(c) Non-Performing Loans to Total and Advances Ratio

This ratio determines the proportion of non-performing loans in the total loan portfolio. Higher ratio implies the bad quality of assets of banks in the form of loans and advances. Hence lower NPL to total credit ratio is preferred. As per international standard only 5% NPL is allowed but in the context of Nepal 10% NPL is acceptable. It is calculated as follows:

$$\text{Non-Performing Loan to Loan and Advances Ratio} = \frac{\text{Non - Performing Loan}}{\text{Loans and Advances}}$$

(d) Loan Loss Provision to Loans and Advances Ratio

This ratio describes the quality of assets in the form of loans and advances that a bank is holding. Since there is risk inherent in loans and advances, NRB has Directed commercial banks to classify its loans into different categories and accordingly to make provision for probable loss. Loan loss provision signifies the cushion against future contingency created by the default of the borrower in payment of loans and ensures the continued solvency of the banks. Since high provision has to be made for non-performing loan, higher provision for loan reflects increasing non-performing loan in volume of total loans and advances. The low ratio signifies the good quality of assets in the volume of loans and advances. It indicates how efficiently it manages loan and advances and makes efforts to cope with probable loan loss. Higher ratio implies, higher portion of NPL in the total loan portfolio. This ratio is calculated as follows:

$$\text{Loan Loss Provision Ratio} = \frac{\text{Loan Loss Provision}}{\text{Total Loan and Advances}}$$

(e) Provision Held to Non-performing loan

This ratio determines the proportion of provision held to non-performing loan of the bank. This ratio measures up to what extent of risk inherent in NPL is covered by the total loan loss provision. Higher ratio signifies that the banks are safeguarded against future contingencies that may create due to non-performing loan or in other words banks have cushion of provision to cope the problem that may be cause to NPL.

Hence higher the ratio better is the financial strength of the bank. This ratio is calculated as follows:

$$\text{Provision Held to Non-Performing Loan} = \frac{\text{Total Loan Loss Provision}}{\text{Non - Performing Loan}}$$

(f) Return on Loans and Advances

This ratio indicates how efficiently the bank has employed its resources in the form of loans and advances. It is the ratio of net profit and total loans and advances of a bank. Net profit refers to that profit which is obtained after all types of deduction like employee bonus, tax, Provision etc. Hence this ratio measures bank's profitability with respect to loans and advances. Higher the ratio better is the performance of the ban. It is calculated as below:

$$\text{Return on Loan and Advances} = \frac{\text{Net Profit}}{\text{Total Loans Advances}}$$

3.5.2 Statistical Tools

Statistical tools are the mathematical techniques used to facilitate the analysis and interpretation of numerical data. "Statistical Analysis is one particular language, which describes the data and makes possible to talk about the relations and the difference of the variables." Following statistical tools have been used in this study.

3.5.2.1 Percentages

A percent is a number of hundredth parts one numbers to another. Uses of percentages make the data much simpler and grasp. It is the simplest statistical device used in interpretation of phenomenon. It can reduce everything to a common base and thereby helps in meaningful presentation. Mathematically, let a represent the base used for comparison of given number in the base may be calculated as:

$$\text{Percentage}(\%) = B \times \frac{100}{A}$$

3.5.2.2 Measures of Central Tendency

Measures of central value are simple statistical treatments of distribution that attempts to find the single figure to describe the entire distribution. It is the best possible value of a group of variables that singly represents to whole group. In the statistical analysis the central value falls with in the approximately middle value of the whole data. Among the several tools of measuring central value, the mean has been used in this analysis where and when necessary. The mean is the arithmetic average of a variable.

Arithmetic Mean of a series is given by

$$Mean\ \left(\overline{X}\right) = \frac{\sum X}{N}$$

3.5.2.3. Measures of Dispersion

Dispersion measures the variation of the data from the central value. The central value alone is not enough to analyze the quality of data regarding its variability. With the light of dispersion, an average becomes more powerful and meaningful. Following tools of measuring dispersion has been used in this study.

a) Standard Deviation

Standard Deviation (S.D.) is the most popular and the most useful measure of dispersion. It indicates the ranges and size of deviance from the middle or mean. It measures the absolute dispersion. Higher the value of standard deviation higher is the variability and vice versa. It is the positive square of average sum of squares of deviations of observations from the arithmetic mean of the distribution. It can be calculated as follows:

$$\text{Standard Deviation } (\sigma) = \sqrt{\frac{\sum\left(X - \overline{X}\right)^2}{N}}$$

b) Coefficient of Variation

The percentage measure of coefficient of standard deviation is called coefficient of variation. The less is the C. V. then more is the uniformity and consistency and vice versa. Standard deviation gives an absolute measure of dispersion. Hence where the mean of the variable is not equal it is not appropriate to compare two pairs of variables based in S.D. only. The coefficient of variation measures the relative measures of dispersion, hence capable to compare two variables independently in terms of their variability.

$$\text{Coefficient of Variation (C.V.)} = \frac{\pm}{\overline{X}} \times 100$$

c) Correlation Coefficient (r)

Correlation refers to the degree of relationship between two variables. Correlation coefficient determines the association between the dependant variable and independent variable. If between the variables, increase or decrease in one cause increase or decrease in another, then such variables are correlated variables. "Correlation may be defined as the degree of linear relationship existing between two or more variables. Two variables are said to be correlated when the changes in the value of one is accompanied by the change of another variable." There are different techniques of calculating correlation coefficient. Among various techniques we have used Karl Pearson coefficient of correlation. It is calculated as follows:

$$\text{Correlation Coefficient (r)} = \frac{\sum xy}{N \pm_x \pm_y}$$

Where,

x = X- $\overline{X}$

y = Y- $\overline{Y}$

σ_x = Standard Deviation of Series X

σ_y = Standard Deviation of Series Y

N = Numbers of Pairs of Observation

On simplification of the equation of r, we obtain the formula for computing r.

$$r = \frac{\sum xy}{\sqrt{\sum X^2 \sum Y^2}}$$

The Karl Pearson Coefficient of correlation always falls between -1 to +1. The value of correlation in minus signifies the negative correlation and in plus signifies the positive correlation.

If,

r = 0, there is no relationship between the variables

r < 0, there is negative relationship between the variables

r > 0, there is positive correlation between the variables

r = +1, the relationship is perfectly positive

r = -1, the relationship is perfectly negative

Probable Error

Probable error of correlation is an old measure testing the reliably of an observed value of correlation coefficient. It is calculated to find the extend to which correlation coefficient is dependable as it depends upon the condition of random sampling probable error of correlation coefficient denoted by P.E. The reliability of the correlation coefficient is judged with the help of probable error (P.E.). It is calculated as follows:

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

Where,

r = Correlation Coefficient

N = No. of Pairs of Observation

If r > 6 P.E., then the correlation coefficient is Significant and reliable

If r < P.E., then the correlation coefficient is insignificant and there is no evidence of correlation

3.5.3 Trend Analysis

Trend analysis is one of the statistical tools, which is used to determine the improvement or determination of its financial situation. Trend analysis informs about the expected future values of various variables. The least square method has been adopted to measure the trend behaviors of these selected banks. The method is widely used in practices. The formula of square method for the straight line is represented by the following formula:

$$Yc = a + bX$$

Where,

Yc = Trend Values

a = Y intercept or the computed trend figure of the Y variable, when X = 0

b = slope of the trend line of the amount of change in Y variable that is associated with change in 1 unit in X variable.

X = Variable that represent time i.e. time variable

The value of the constants a and b can be determined solving the following two normal equations:

$$\sum Y = Na + b \sum X$$

$$\sum XY = a\sum X + b \sum X$$

Where,

N = number of years

But for simplification, if the time variable is measured as a deviation from its mean i.e. mid point is taken as origin, the negative value in the first half of the series balance out of the positive values in the second half of so that the values of constant a and b can easily determined by using following formula:

$$a = \frac{\sum X}{N}$$

$$b = \frac{\sum Y}{N}$$

3.5.4 Diagrammatic and Graphical Representation

Diagrams and graphs are visual aids that give a bird eye view of a given set of numerical data. They represent the data in simple and readily compromise form. Hence various bar diagrams, pie charts and graph have been used for presentation and analysis of data.

After highlighting the research methodology, the next chapters content the presentation and analysis of data of concerned financial institution.

CHAPTER – FOUR

DATA PRESENTATION AND ANALYSIS

This chapter deals with the presentation, analysis and interpretation of relevant data and information of NIBL and HBL. Also, the analysis and interpretation of the information and data produced from various reports is also contained in this chapter. To obtain best result, the data and information have been analyzed according to the research methodology as mentioned in the Chapter 3.

The main purpose of analyzing the data is to change it from an unprocessed form to an understandable presentation. The analysis of data consists of organizing, tabulating, and performing statistical analysis. (Wolff & Pant, 2007)

The collected data and information are presented in this section. Various tables, charts and graphs are used to best present the data. The data and information has been presented in most understandable format.

This chapter is partitioned into the sections of (1) Ratio Analysis, (2) Correlation Analysis, (3) Trend Analysis, (4) Loan Classification Analysis, and (5) Major Findings.

4.1 Ratio Analysis

4.1.1 Loan and Advances to Total Asset Ratio of NIBL & HBL

The ratio of loan and advances to total assets measures the volume of loan and advances in the structure of total assets. The high degree of ratio indicates the good performance of the banks in mobilizing its fund by way of lending functions. However in its reverse side, the high degree is representative of low liquidity ratio. Granting loan and advances always carries a certain degree of risk. Thus this asset of banking business is regarded as risky assets. Hence this ratio measures the management attitude towards risky assets. The low ratio is indicative of low productivity and high degree of safely in liquidity and vice versa.

Table 4.1

Loan and Advances to Total Asset Ratio of NIBL & HBL

(Rs. in Million)

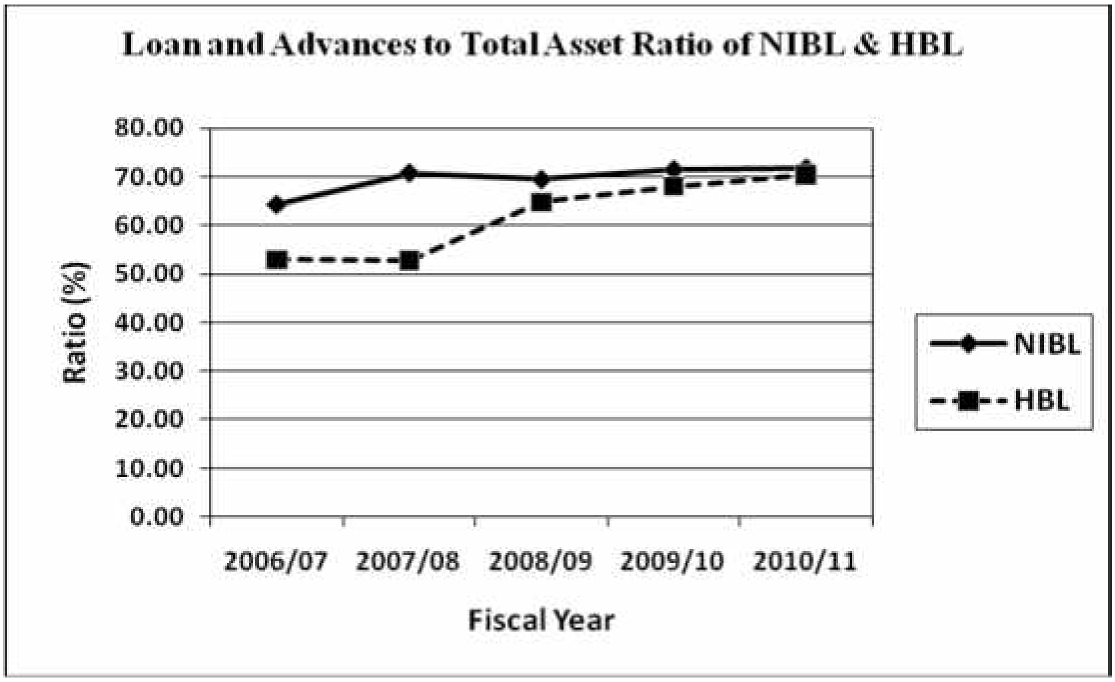
Fiscal Year	NIBL			HBL		
	Loan & Advances	Total Asset	Ratio (%)	Loan & Advances	Total Asset	Ratio (%)
2006/07	17,769.10	27,590.84	64.40	17,793.72	33,519.14	53.09
2007/08	27,529.30	38,873.31	70.82	20,179.61	38,175.53	52.86
2008/09	36,827.16	53,010.80	69.47	25,519.52	39,320.32	64.90
2009/10	40,948.44	57,305.41	71.46	29,123.75	42,717.12	68.18
2010/11	41,887.69	58,356.83	71.78	32,968.27	46,736.20	70.54
Mean			**69.59**	**Mean**		**61.91**
S. D.			**2.71**	**S. D.**		**7.52**
C. V.			**3.89**	**C. V.**		**12.14**

The table no. 4.1 shows the loan and advances to total asset of the two banks for five consecutive years. The ratio is in the fluctuating trends. The overall ratio of the two banks has been ranged from 52.86% of HBL in 2007/08 to 71.78% in 2010/11 of NIBL. The mean ratio of NIBL and HBL are 69.59% and 61.91% respectively. Hence among two banks NIBL has the highest proportion of loan and advances in the total asset structure. It means the HBL has the lowest degree of investment in risky asset. The management of HBL is risk averse as they invested in risk free asset. The Directors' Credit Committee (DCC) of HBL puts in a place a suitable monitoring mechanism ensuring a healthy loan portfolio limiting concentration risk and the same time providing an independent review of the credit portfolio of the bank.

The standard deviation of NIBL & HBL 2.71% & 7.52% and C.V's are 3.89% & 12.14 % respectively. Thus it can be interpreted that HBL has the higher deviation with higher degree of variation in this ratio. Even though this ratio is least of NIBL, it has the most consistent ratio and the least deviation during the study period. The ratio of NIBL is higher than the HBL because of increasing trend of Loan and advances than NIBL. Following figure shows the loan and advances to total asset ratio of NIBL and HBL.

Figure 4.1

Loan and Advances to Total Asset Ratio of NIBL & HBL



4.1.2 Loan and Advances to Total Deposit Ratio of NIBL & HBL

This ratio is often called Credit Deposit ratio (CD ratio). The core banking function is to mobilize the funds obtained from the depositors to borrowers and earn profit and CD ratio is the fundamental parameter to ascertain fund deployment efficiency of commercial bank. In other words this ratio is calculated to find out how successfully the banks are utilizing their total deposits on credit of loan and advances for profit generating purpose as loan and advances yield high rate of return. Greater CD ratio implies the better utilization of total deposits and better earning, however, liquidity requirements also needs due consideration. Hence 70%-80% CD ratio is considered as appropriate. This ratio is calculated by dividing total credit of loan and advances by total deposit of the bank.

Table 4.2

Loan and Advances to Total Deposit Ratio of NIBL & HBL

(Rs. in Million)

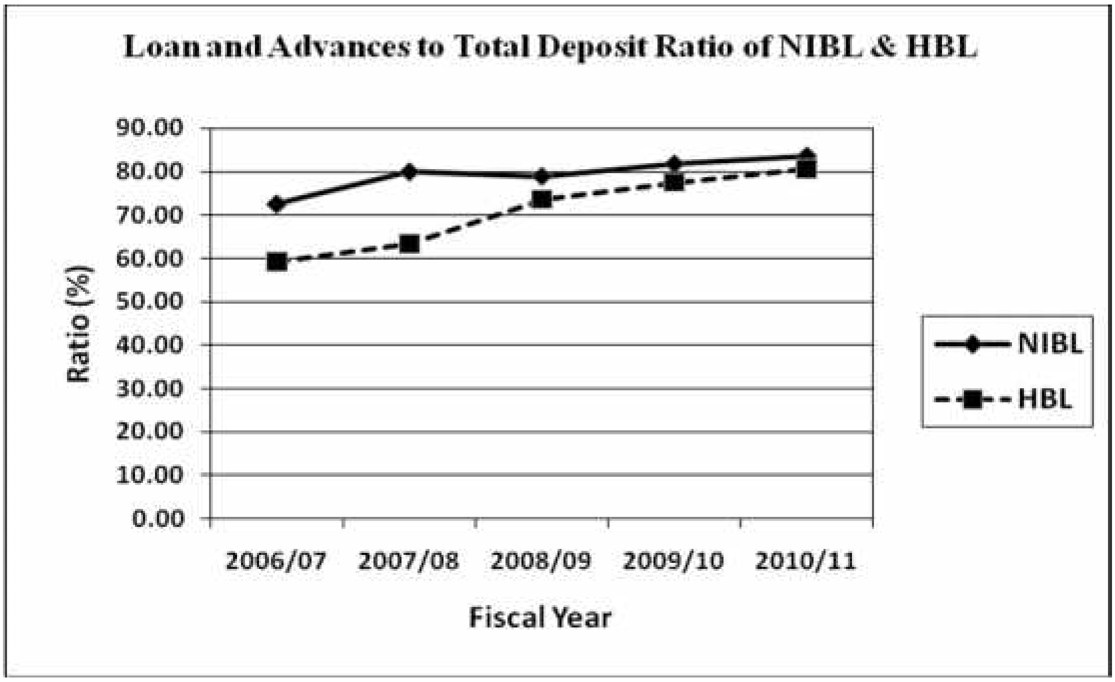
Fiscal Year	NIBL			HBL		
	Loan & Advances	Total Deposit	Ratio (%)	Loan & Advances	Total Deposit	Ratio (%)
2006/07	17,769.10	24,488.86	72.56	17,793.72	30,048.42	59.22
2007/08	27,529.30	34,451.73	79.91	20,179.61	31,842.79	63.37
2008/09	36,827.16	46,698.10	78.86	25,519.52	34,681.35	73.58
2009/10	40,948.44	50,094.73	81.74	29,123.75	37,611.20	77.43
2010/11	41,887.69	50,138.12	83.54	32,968.27	40,920.63	80.57
Mean			**79.32**	**Mean**		**70.83**
S. D.			**3.74**	**S. D.**		**8.20**
C. V.			**4.72**	**C. V.**		**11.58**

The table no. 4.2 shows the loan and advances to total deposit of two banks for five consecutive years. The ratio of the selected banks is fluctuating all over the observation period. The ratio is least i.e. 59.22% of HBL in 2006/07 and highest i.e. 83.54% of NIBL in 2010/11. The mean ratio is 79.32% and 70.83% of NIBL and HBL respectively. However NIBL has the highest proportion of loan and advances in the total deposit. It signifies that NIBL has been ahead in utilizing depositors' money on loan and advances with the objective of profit maximization. The management of HBL is risk averse as they invested in risk free asset.

The standard deviation of NIBL and HBL are 3.74 & 8.20 and C.V's are 4.72 and 11.58 respectively. Thus it signified that HBL has higher deviation with higher degree of variation in this ratio than NIBL. Following figure shows the loan and advances to total deposit ratio of NIBL and HBL.

Figure 4.2

Loan and Advances to Total Deposit Ratio of NIBL & HBL



4.1.3 Non-Performing Loan to Total Loan and Advances Ratio of NIBL & HBL

This ratio is the proportion of non-performing loan in the total loan portfolio. As per NRB directives the Loan falling under category of substandard, doubtful and loss are regarded as non-performing loan. Higher ratio implies the bad quality of assets of banks in the form of Loan and advances. Hence lower NPL to total credit ratio is preferred. As per international standard only 5 % NPL is allowed but in the context of Nepal maximum 10% NPL is acceptable.

Table 4.3

NPL to Loan and Advances Ratio of NIBL & HBL

(Rs. in Million)

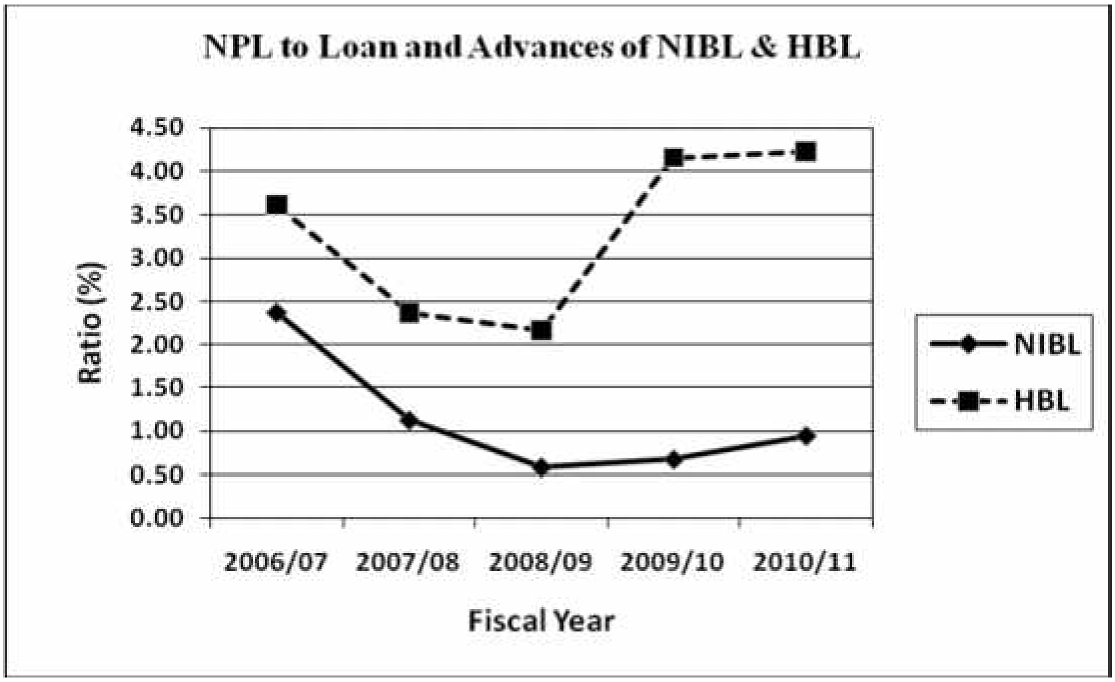
Fiscal Year	NIBL			HBL		
	NPL	Loan & Advances	Ratio (%)	NPL	Loan & Advances	Ratio (%)
2006/07	421.97	17,769.10	2.37	641.62	17,793.72	3.61
2007/08	309.47	27,529.30	1.12	477.23	20,179.61	2.36
2008/09	213.91	36,827.16	0.58	551.31	25,519.52	2.16
2009/10	274.33	40,948.44	0.67	1,208.12	29,123.75	4.15
2010/11	395.28	41,887.69	0.94	1,391.75	32,968.27	4.22
Mean			**1.14**	**Mean**		**3.30**
S. D.			**0.65**	**S. D.**		**0.88**
C. V.			**56.87**	**C. V.**		**26.54**

The table no. 4.3 exhibits the ratio of non-performing loan to loan and advances of NIBL and HBL for five consecutive years. The figure present in the above table shows that HBL has the highest ratio than NIBL in consecutive years. NIBL is successful to reduce its NPL to Loan and advances ratio during 2006/07 to 2008/09 but it increase in 2009/10 and 2010/11 than previous year. However HBL also reduce its NPL to loan and advances ratio during 2006/07 to 2008/09 then it increase in 2009/10 and 20010/11. Both banks are decreasing trend up to 2008/09 then few percentage are increasing it. Any way NPL of both banks is maintain lowest than 5% that is the result of effective credit management of banks and its efforts of recovering bad debts through establishment of recovery cell. The overall ratio has been ranged from 0.58% on NIBL in 2008/09 and 4.22% of HBL in 2010/11. The mean of non-performing loan to total loan ratio of NIBL and HBL are 1.14% and 3.30% respectively. The NPL of HBL is higher than NIBL in all consecutive years so the loan and advances of NIBL than HBL is higher quality but the ratio of both bank are in acceptable manner.

The standard deviation of NIBL and HBL are 0.65 and 0.88 and C.V's are 56.87 & 26.54 respectively. This it signified that HBL has the highest deviation and lower degree of variation. Since NPL is one of the most important causes of banking crisis, both bank should give serious attention to this matter. Following figure shows the NPL to Loan and Advances ratio.

Figure 4.3

NPL to Loan and Advances Ratio of NIBL & HBL



4.1.4 Loan Loss Provision to Total Loan and Advances Ratio of NIBL & HBL

This ratio describes the quality to assets in the form of loan and advances that a bank is holding. Since there is risk inherent in Loan and advances, NRB has directed commercial banks to classify its loans into different categories and accordingly to make provision for probable loss. Loan loss provision signifies the cushion against future contingency created by default of the borrower in payment of loans and ensures the continued solvency of the banks. Since high provision has to be made for non-performing loan, higher provision for loan loss reflects increasing non-performing loan in volume of total loan and advances. It indicates how efficiently it manages loan and advances and makes efforts to cope with probable loan loss. Higher ratio implies, higher portion of NPL in the total loan portfolio.

Table 4.4

LLP to Loan and Advances Ratio of NIBL & HBL

(Rs. in Million)

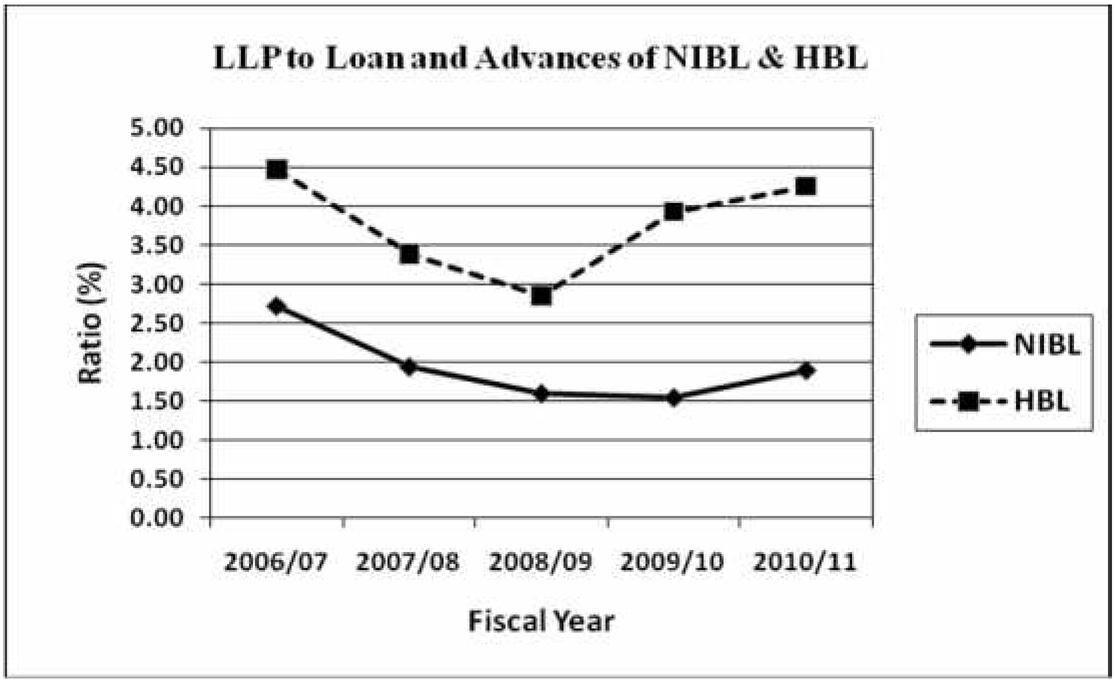
Fiscal Year	NIBL			HBL		
	LLP	Loan & Advances	Ratio (%)	LLP	Loan & Advances	Ratio (%)
2006/07	482.67	17,769.10	2.72	795.73	17,793.72	4.47
2007/08	532.65	27,529.30	1.93	682.09	20,179.61	3.38
2008/09	585.95	36,827.16	1.59	726.36	25,519.52	2.85
2009/10	630.13	40,948.44	1.54	1,143.13	29,123.75	3.93
2010/11	792.18	41,887.69	1.89	1,401.29	32,968.27	4.25
Mean			**1.93**	**Mean**		**3.77**
S. D.			**0.42**	**S. D.**		**0.59**
C. V.			**21.78**	**C. V.**		**15.69**

The table no. 4.4 exhibits the ratio of loan loss provision to loan and advances of NIBL and HBL for five consecutive years. The figure presented in the above table shows that HBL has the highest ratio during the study period. The ratios of NIBL are decreasing in 2006/07 to 2009/10 but in increasing in 2010/11. Similarly ratios of HBL are decreasing in 2006/07 to 2008/09 and it increasing in 2009/10 to 2010/11. The overall ratio has been ranged from 1.54% of NIBL in 2009/10 to 4.47% of HBL in 2006/07. The mean ration of LLP to Loan and advances of NIBL and HBL are 1.93% and 3.77% respectively. Higher LLP is indicative of poor and ineffective credit policy, higher proportion of non-performing loan and poor performance of the economics. The greater ratio of HBL in 2006/07 shows the higher proportion on non-performing loan in total loans but it is decreasing throughout the years. Both bank’s loan loss provision is fluctuating trend it explain that both bank has been successful to reduce its non-performing loan resulting to decreasing loan loss provision in some previous fiscal years but by various factor, the ratio are increasing in last fiscal year. So both bank should be try to decrease non-performing loan then reduce the loan loss provision as per total loan.

The standard deviation of NIBL and HBL are 0.42 & 0.59 and C.V.'s are 21.78 & 15.69 respectively. Among two banks, NIBL has least deviation and highest degree of variability of ratio during the study period. Following figure shows the LLP to Loan and Advances ratio.

Figure 4.4

LLP to Loan and Advances Ratio of NIBL & HBL



4.1.5 Provision Held to Non-Performing Loan Ratio of NIBL & HBL

This ratio determines the proportion of provision held to non-performing loan of the bank. This ratio measures up to what extant of risk inherent in NPL is covered by the total loan loss provision. Higher ratio signifies that the banks are safeguarded against future contingencies that may create due to non-performing loan or in other words banks have cushion of provision to cope the problem that may be cause due to NPL. Hence higher the ratio better is the financial position of the bank.

Table 4.5

LLP to NPL Ratio of NIBL & HBL

(Rs. in Million)

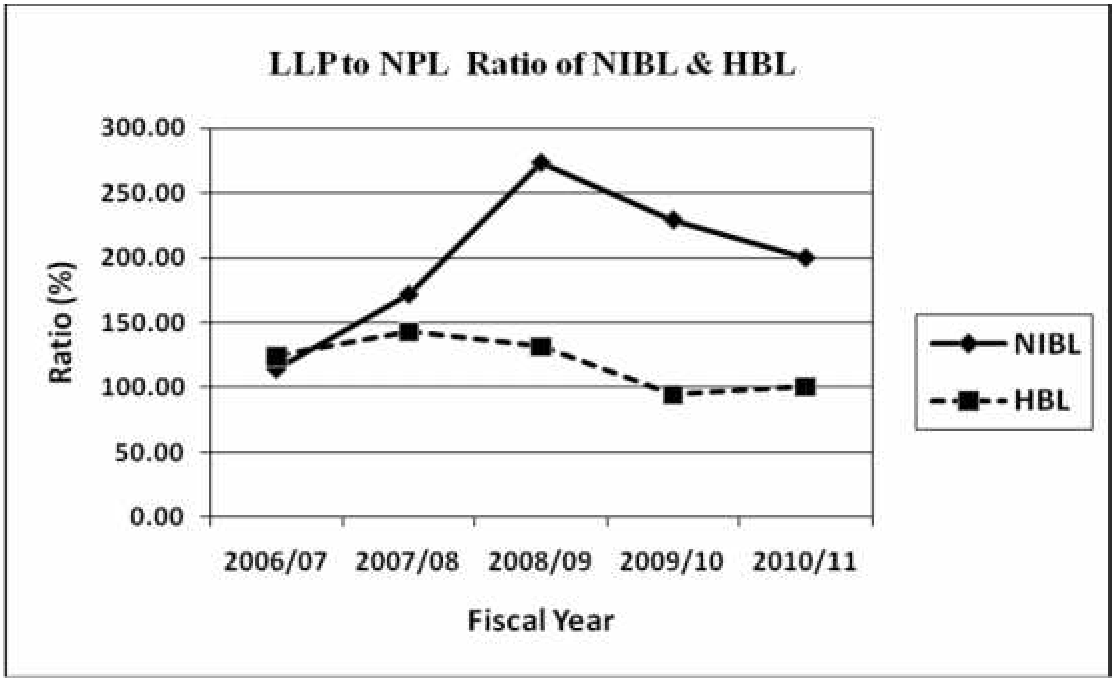
Fiscal Year	NIBL			HBL		
	LLP	**NPL**	**Ratio (%)**	**LLP**	**NPL**	**Ratio (%)**
2006/07	482.67	421.97	114.38	795.73	641.62	124.02
2007/08	532.65	309.47	172.12	682.09	477.23	142.93
2008/09	585.95	213.91	273.92	726.36	551.31	131.75
2009/10	630.13	274.33	229.70	1,143.13	1,208.12	94.62
2010/11	792.18	395.28	200.41	1,401.29	1,391.75	100.69
Mean			**198.11**	**Mean**		**118.80**
S. D.			**53.73**	**S. D.**		**18.38**
C. V.			**27.12**	**C. V.**		**15.47**

The table no. 4.5 exhibits the ratio of provision held to non-performing loan of NIBL and HBL for the five consecutive years. The figure represented in the above table shows that NIBL has the highest ratio during the period. The overall ratio has been ranged from 94.62% HBL in 2009/10 to 273.92% of NIBL in 2008/09. The mean ratio of NIBL and HBL are 198.11% and 118.80% respectively. The ratio of NIBL is significantly high in comparison of HBL and portrays that the banks has adequate provision against non-performing loan.

The standard deviation of NIBL and HBL are 53.73 & 18.38 and C.V.'s are 27.12 and 15.47 respectively. Thus it signifies that NIBL has highest deviation along with the highest degree of variation in this ratio. Following figure shows the Loan Loss Provision to Non-Performing Asset in Chart.

Figure 4.5

LLP to NPL Ratio of NIBL & HBL



4.1.6 Return on Loan and Advances of NIBL & HBL

This ratio indicates how efficiently the bank has employed its resources in the form of loan and advances. This ratio is calculated by dividing net profit of the bank by total loan and advancers. Net profit refers to that profit which is obtained after all types of deduction like employees bonus, tax, provision etc. hence this ratio measures bank's profitability with respect to loan and advances. Higher the ratio better is the bank performance.

Table 4.6

Net Profit to Loan and Advances Ratio of NIBL & HBL

(Rs. in Million)

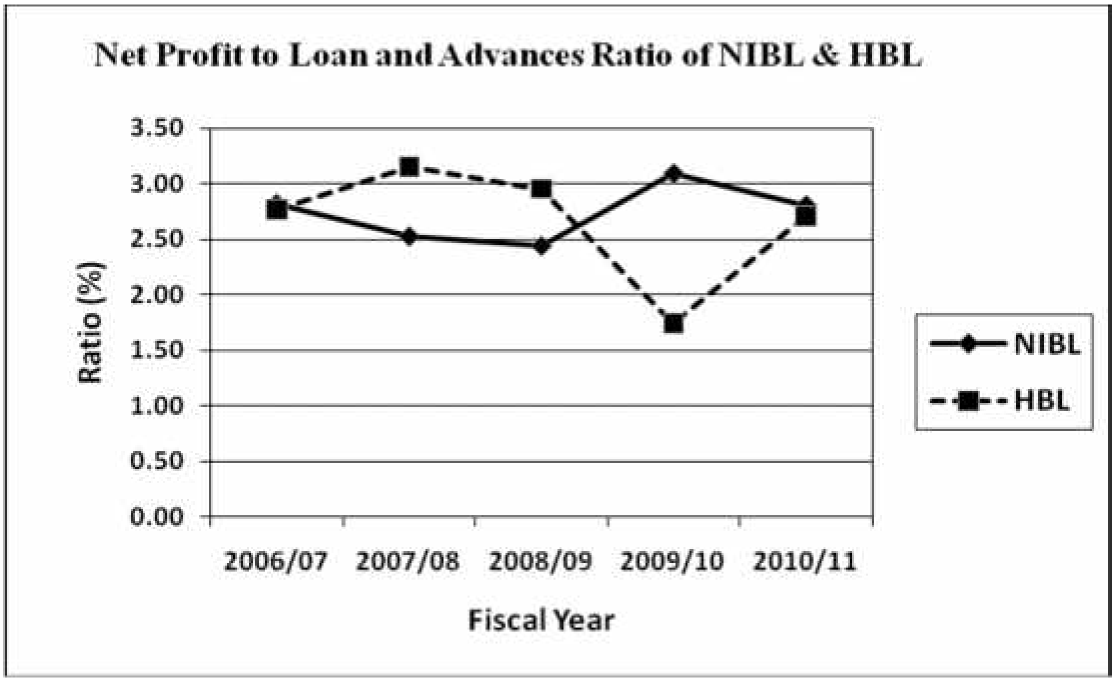
Fiscal Year	**NIBL**			**HBL**		
	Net Profit	**Loan & Advances**	**Ratio (%)**	**Net Profit**	**Loan & Advances**	**Ratio (%)**
2006/07	501.40	17,769.10	2.82	491.82	17,793.72	2.76
2007/08	696.73	27,529.30	2.53	635.87	20,179.61	3.15
2008/09	900.62	36,827.16	2.45	752.83	25,519.52	2.95
2009/10	1,265.95	40,948.44	3.09	508.80	29,123.75	1.75
2010/11	1,176.64	41,887.69	2.81	893.11	32,968.27	2.71
Mean			**2.74**	**Mean**		**2.66**
S. D.			**0.23**	**S. D.**		**0.48**
C. V.			**8.41**	**C. V.**		**18.17**

The table no. 4.6 exhibits the ratio of return on loan and advances of NIBL and HBL for five consecutive years. The figure represented in the above table shows that HBL has the highest ratio during the study period. The ratio of both banks is fluctuating. The overall ratio is minimum 1.75% in 2009/10 and maximum 3.15% in 2007/08 of HBL. The ratios of NIBL are decreasing in 2006/07 to 2008/09 i.e. 2.82% to 2.45% and then increases to 3.09% in 2009/10 but again decreases to 2.81% in 2010/11. Similarly, the ratio of HBL is 2.76% in 2006/07 and then increases to 3.15% in 2007/08 but then decreases to 2.95% and 1.75% in 20089/09 and 2009/10 respectively but again it increases to 2.71% in 2010/11. The mean ratios of both banks are 2.74% and 2.66% respectively. Since the profit ratio of both banks are similarly.

The standard deviation of NIBL and HBL are 0.23 & 0.48 and C.V's are 8.41 & 18.17 respectively. It signifies HBL has the highest deviation and higher degree of variation in this ratio. Thus it can be concluded that both bank has the highest exposure of Loan and advances with the highest profit. Although comparatively, NIBL has gain more profit by lending its recourses than the other comparative bank HBL. Following figure shows the Net Profit to Loan and Advances ratio in chart.

Figure 4.6

Net Profit to Loan and Advances Ratio of NIBL & HBL



4.2 Correlation Analysis

The percentage measure of coefficient of standard deviation is called coefficient of variation. The less is the C.V. then more is the uniformity and consistency and vice versa. Standard deviation gives an absolute measure of dispersion. Hence where the mean of the variable is not equal it is not appropriate to compare two pairs of variables based in S.D. only. The coefficient of variation measures the relative measures of dispersion, hence capable to compare two variables independently in terms of their variability.

4.2.1 Correlation between Loan Loss Provision and Loan and Advances

The correlation between LLP and loan and advances shows the degree of relationship between these two items. How a unit increment in Loan and advances affect the loan loss provision measured by this correlation. Here loan and advances is independent variable and LLP is dependent variable. (Appendix D, E)

Table 4.7

Correlation between Loan Loss Provision and Loan and Advances

Bank	Correlation Coefficient (r)	Probable Error (P.E.)	6 * P.E.
NIBL	0.8345	0.0916	0.5496
HBL	0.8605	0.0783	0.4698

The table no.4.7 explains that the relationship between Loan and advances and LLP. Here the correlation of NIBL and HBL are 0.8345 and 0.8605 respectively and both are more than 6 times the value of its P.E. i.e. 0.5496 and 0.4698 respectively. The probable error (P.E.) of NIBL and HBL are 0.0916 and 0.0783 respectively. So, there is positive correlation between LLP and loan and advances of both bank NIBL and HBL during the study period and its correlation coefficient is significant and reliable. So it can be interpreted that there is high degree of positive correlation between LLP and loan and advances of NIBL and HBL.

4.2.2 Correlation between Loan Loss Provision and Non-Performing Loan

The correlation between LLP and non-performing loan describes the relationship between LLP and NPL. How a unit increases in NPA effect the LLP is exhibited by this correlation. Here non-performing asset is independent variable and LLP is dependent variable. As earlier mentioned NPA are the loan falling on the category of substandard, doubtful and bad loan and the respective provisioning requirement is 25%, 50% and 100%. Higher the NPL higher will be the provisioning amount. (Appendix D, E)

Table 4.8

Correlation between Loan Loss Provision and Non-performing Loan

Bank	Correlation Coefficient (r)	Probable Error (P.E.)	6 * P.E.
NIBL	0.0800	0.2997	1.7982
HBL	0.9900	0.0060	0.0360

The table no.4.8 explains the relationships between LLP and NPL. Here two banks have positive correlation between NPL and LLP. That means increment in NPL leads to increment in LLP. The correlation coefficient of NIBL is 0.0800 and its P.E and 6 times of P.E. are 0.2997 and 1.7982. The correlation coefficient is lower than the value of P.E. Hence correlation coefficient between LLP and NPL of NIBL is insignificant and there is no evidence of correlation. In case of HBL r is higher than 6 times the value of P.E. The value of correlation coefficient is 0.9900. The value of P.E. and 6.P.E of HBL are 0.0060 and 0.0360 respectively. Hence its correlation coefficient is said to be significant and reliable. So it can be interpreted that there is high degree of positive correlation between NPL and LLP on HBL.

4.2.3 Correlation between Loan and Advances and Total Deposit

Deposit is one of the major items of liability side and loan and advances is the major item of the asset side of balance sheet of a commercial bank. Bank utilized the collected fund from the depositors in the form of Loan and advances. The correlation coefficient between loan and advances and deposit describes the degree of relationship between these two variables. Here deposit is the independent variable and Loan and advances is dependent variable. Hence how a unit increase in deposit impact in the volume of Loan and advances is exhibited by this correlation coefficient. (Appendix D,E)

Table 4.9

Correlation between Loan and Advances and Total Deposit

Bank	Correlation Coefficient (r)	Probable Error (P.E.)	6 * P.E.
NIBL	0.9972	0.0017	0.0102
HBL	0.9954	0.0027	0.0162

The table no. 4.9 shows the correlation coefficient, probable error and six times value of P.E. between loan and advances and total deposit of two banks. It shows there is positive correlation between loan and advances and deposit of NIBL and HBL. The respective value of correlation coefficient of NIBL and HBL are 0.9972 and 0.9954, P.E.'s are 0.0017 and 0.0027 and 6P.E. are 0.0102 and 0.0162 respectively. The correlation coefficient of both banks are greater than their six times value of P.E. hence it can be concluded that correlation between these two variables in NIBL and HBL is certain and significant. There is high degree correlation between loan and advances and total deposit of both banks. That means increment in volume of deposit leads to increment in Loan and advances. However, the deposit and Loan and advances of HBL has lesser degree of relationship in comparison to NIBL.

4.3 Trend Analysis

Trend analysis is a statistical tool, which helps to forecast the future values of different variables on the basis of past tendencies of variable. Trend analysis informs about the expected future values of various variables. Amongst the various methods to determine trend the least square method is widely used in practices. Hence in this study also least square method has been adopted to measure the trend behaviors of these selected banks. However, trend analysis is based on the assumption that past tendencies continues in the future. Under this heading the effort has been made to calculate trend values of following variables from mid July 2007 to mid July 2011.

4.3.1 Trend Analysis of Loan and Advances of NIBL & HBL

The values of average loan and advances (a), rate of change of Loan and advances (b) and trend values of Loan and advances of two banks for ten years from mid July 2007 to mid July 2016 are as follows (Appendix F,G)

Table 4.10

Trend Values of Loan & Advances of NIBL & HBL

(Rs. in Million)

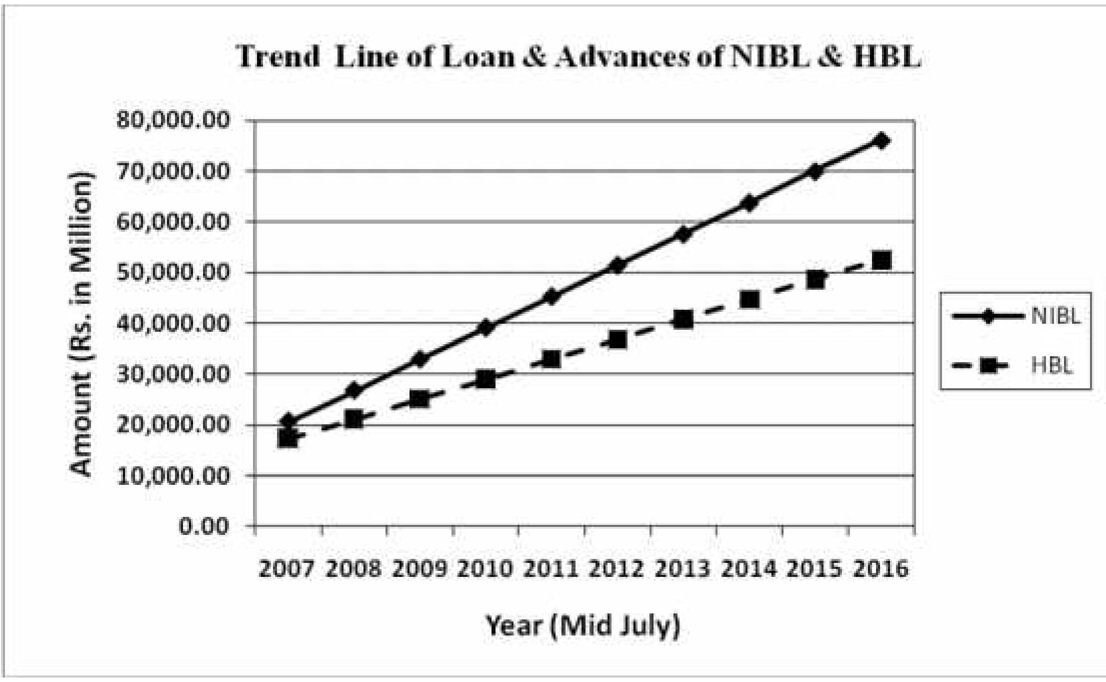
Year (Mid July)	NIBL a = 32,992.34 b = 6,165.63	HBL a = 25,116.97 b = 3,929.32
2007	20,661.07	17,258.33
2008	26,826.71	21,187.65
2009	32,992.34	25,116.97
2010	39,157.97	29,046.30
2011	45,323.60	32,975.62
2012	51,489.23	36,904.95
2013	57,654.87	40,834.27
2014	63,820.50	44,763.59
2015	69,986.13	48,692.92
2016	76,151.76	52,622.24

The table no. 4.10 shows that both banks have the increasing trend of loan and advances. The average loan and advances of NIBL is Rs. 32,992.34 million and increasing every year at the rate of Rs. 6,165.63 million. Hence expected loan and advances of NIBL are supposed to increase from Rs. 51,489.23 million in 2012 to 76151.76 million in 2016. The average loan and advances of HBL is Rs. 25,116.97 million which increase by Rs. 3,929.32 million every year. Accordingly Loan and advances of HBL is expected to increase from Rs. 3,6904.95 million in 2012 to Rs. 52622.24 million in 2016.

Both the bank's trend line of loan and advances shows that in increasing trend of Loan and advances but NIBL has higher rate of increment than that of HBL. From this it can be conclude that HBL has policy of low investment in loan and advances than NIBL. Following figure no.7 represent the trend line of Loan and advances of two banks for ten consecutive years.

Figure 4.7

Trend Line of Loan and Advances of NIBL & HBL



4.3.2 Trend Analysis of Non-Performing Loan of NIBL & HBL

The calculated values of average Non-Performing Loan (a) rate of change of NPL, and (b) trend values of NPL for 10 years from mid July 2007 to mid July 2016 are as follows (Appendix F, G)

Table 4.11

Trend Values of Non-Performing Loan of NIBL & HBL

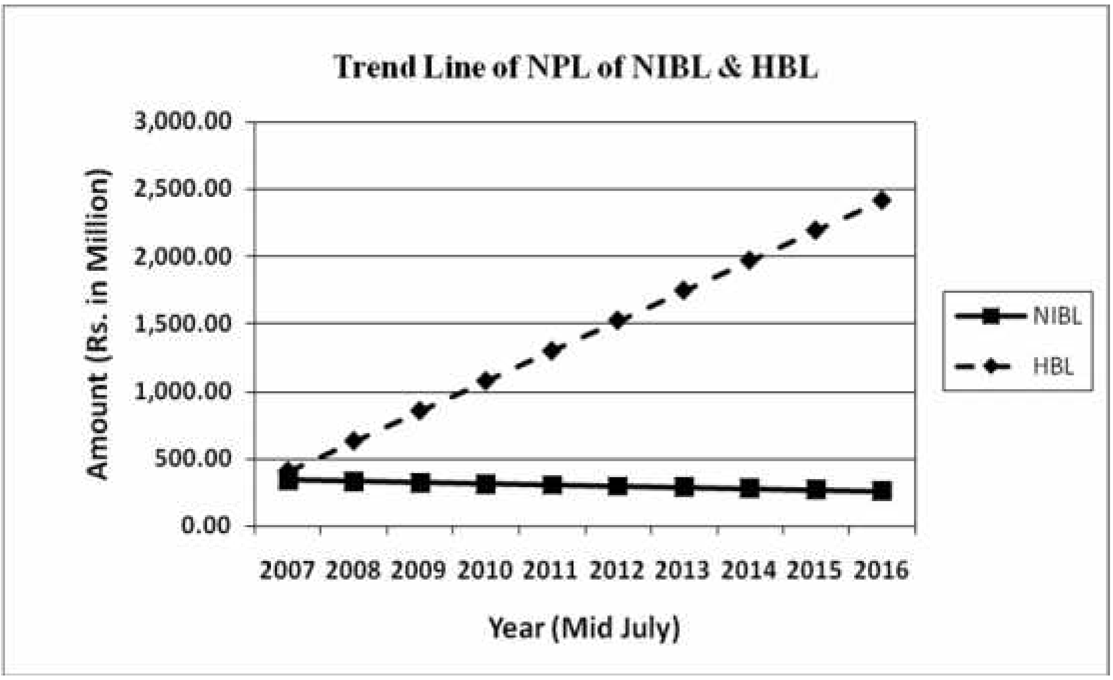
(Rs. in Million)

Year (Mid July)	NIBL a = 322.99 b = -8.85	HBL a = 854.01 b = 223.12
2007	340.70	407.78
2008	331.84	630.89
2009	322.99	854.01
2010	314.14	1,077.12
2011	305.29	1,300.24
2012	296.44	1,523.35
2013	287.58	1,746.47
2014	278.73	1,969.58
2015	269.88	2,192.70
2016	261.03	2,415.81

The table no. 4.11 shows that NIBL has decreasing trend but HBL has increasing trend of Non-Performing Loan. The average NPL of NIBL 322.99 million, which is decreasing at the rate of Rs. 8.85 million each year. Hence the expected NPL of NIBL is supposed to decrease from Rs. 296.44 million in 2012 to Rs. 261.03 million in 2016. The decreasing trend of NPL of NIBL shows that the NIBL has successes to reduce non-performing loan. Due to NIBL's recovery efforts through establishment of recover cell, its NPL has come down in recent years. Hence NIBL shows decreasing trend of NPL. This may be due to good credit control system of NIBL. But in case of HBL, the average NPL is Rs. 854.01 million which is increasing every year at the rate of Rs. 223.12 million. The expected NPL of HBL is Rs. 1523.35 million in 2012, which is increase to Rs. 2,415.81 Million in 2016. If this trend continues, HBL will severally affected by the problem of increasing non-performing loan. Following figure represent the trend line of non-performing loan of two banks for 10 consecutive years.

Figure 4.8

Trend Line of NPL of NIBL& HBL



4.3.3 Trend Analysis of Loan Loss Provision of NIBL & HBL

The calculated values of average loan loss provision (a) rate of change of LLP, and (b) trend values of LLP for 10 years from mid July 2007 to mid July 2016 of the two banks are as follows (Appendix F, G)

Table 4.12

Trend Values of Loan Loss Provision of NIBL & HBL

(Rs. in Million)

Year (Mid July)	**NIBL** **a = 604.72** **b = 71.65**	**HBL** **a = 949.72** **b = 167.22**
2007	461.42	615.29
2008	533.07	782.50

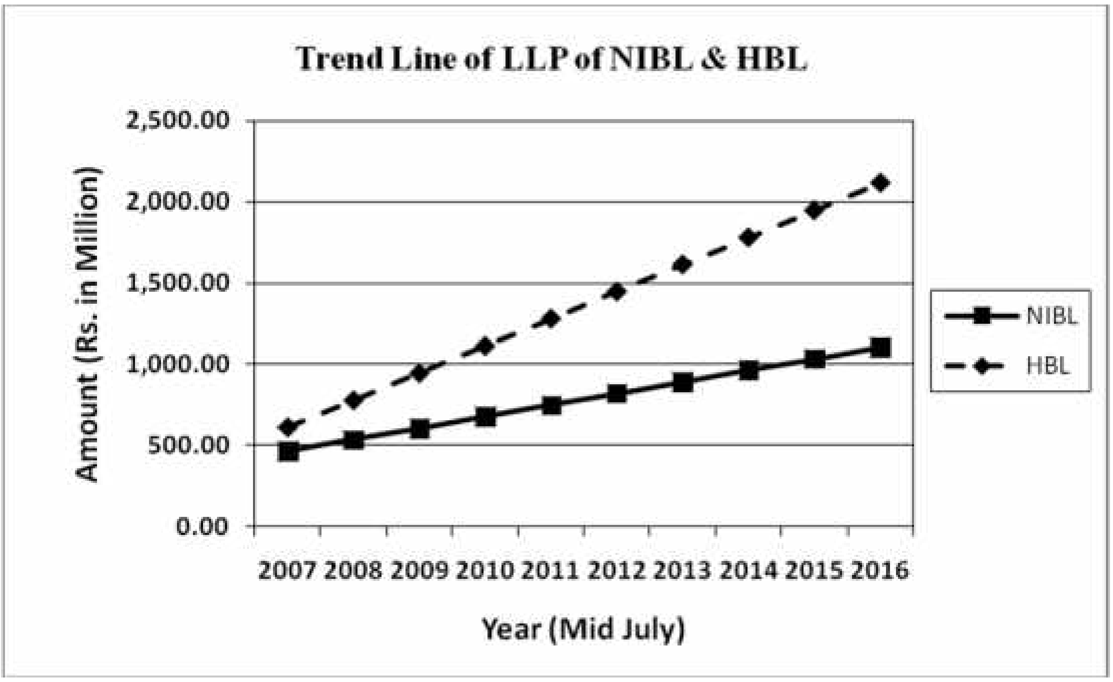
2009	604.72	949.72
2010	676.37	1,116.94
2011	748.02	1,284.15
2012	819.67	1,451.37
2013	891.32	1,618.58
2014	962.97	1,785.80
2015	1,034.62	1,953.02
2016	1,106.27	2,120.23

The above table no. 4.12 shows that both bank NIBL and HBL have increasing trend of LLP. The average LLP of NIBL is Rs. 604.72 million which is increasing every year at the rate of Rs. 71.65 million. Hence the expected LLP of NIBL is supposed to increase to Rs. 819.67 million in 2012 and Rs. 1,106.27 million in 2016. The average LLP of HBL is Rs. 949.72 million which is increasing every year at the rate of Rs. 167.22 million. Hence the expected LLP of HBL is supposed to Rs. 1,451.37 million in 2012 which is increased to Rs. 2,120.23 million in 2016. The increasing trend of LLP of NIBL and HBL is due to the increasing trend of Loan and advances in total asset.

In comparison to both banks, trend line of LLP of NIBL is less increasing than HBL. It shows that NIBL is successful to control to increase non-performing loan than HBL. The increasing trend value of LLP indicates the increment of NPL in total asset quality. Following figure no. 4.9 shows that the trend line of LLP of both banks for 10 consecutive years.

Figure 4.9

Trend Line of LLP of NIBL & HBL



4.3.4 Trend Analysis of Net Profit of NIBL & HBL

The calculated values of average Net Profit (a) rate of change of Net Profit, and (b) trend values for ten years from mid July 2007 to mid July 2016 of the two banks are as follows (Appendix F, G)

Table 4.13

Trend Values of Net Profit of NIBL & HBL

(Rs. in Million)

Year (Mid July)	NIBL a = 908.27 b = 191.97	HBL a = 656.49 b = 67.55
2007	524.33	521.38
2008	716.30	588.94
2009	908.27	656.49

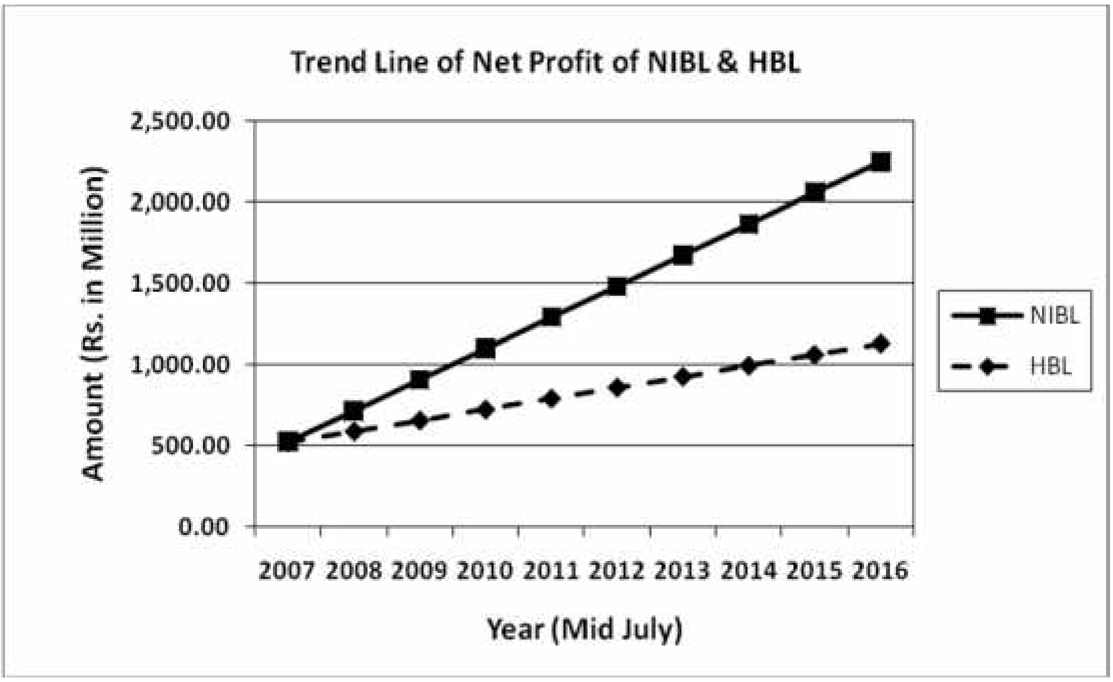
2010	1,100.24	724.04
2011	1,292.21	791.59
2012	1,484.18	859.14
2013	1,676.15	926.69
2014	1,868.12	994.24
2015	2,060.09	1,061.79
2016	2,252.06	1,129.34

The above table no. 4.13 shows that both banks have the increasing trend of net profit. The average net profit of NIBL is Rs. 908.27 million and increasing every year at the rate of Rs. 191.97 million. Hence expected net profit of NIBL is supposed to increase from Rs. 1,484.18 million in 2012 to Rs. 2,252.06 million in 2016. The average net profit of HBL is Rs. 656.49 million which increase by Rs. 67.55 million every year. Hence, expected that net profit of NIBL is supposed to increase from Rs. 859.14 million in 2012 to Rs. 1,129.34 million in 2016.

The above figure depicts that NIBL is ahead of in generating net profit and its rate of increment of net profit is higher than that of HBL. Following figure no. 4.10 represent the trend line of net profit of two banks for 10 consecutive years.

Figure 4.10

Trend Line of Net Profit of NIBL & HBL



4.4 Analysis of Classification of Loan and Provisioning as per New Directives

As per the new directive, loan and advances are to be classified into four categories namely Pass, Substandard, Doubtful and Loss with respective provisioning 1%, 25%, 50% and 100% on the basis of ageing of past dues. Besides this in case of insured priority and deprived sector loan, the provisioning requirement is one-fourth of that of normal loan loss provisioning requirement. Hence the respective provisioning requirement for pass, substandard, doubtful and loss loan are 0.25%, 6.25%, 12.5% and 25% of the outstanding loan. In case of rescheduled or restructured or swapped loan, if such loans fall under pass category, the minimum provisioning requirement is 12.5% and if this is the case of priority sector loan, 3.125% provisioning should be provided for probable loss. Further if the loan is granted only against personal guarantee, where the loan falls under the category of pass, substandard and doubtful, in addition to the normal loss provision applicable for the category, an additional 20% must be provided. Hence in this case the provisioning required for pass, substandard and doubtful is 21%, 45% and 70% respectively. Hence it can be concluded that loan loss provision required for different category of loan ranges as follows:

Loan Category	Loan Loss Provision (Ranges From)
Pass	0.25% to 21.00%
Substandard	6.25% to 45.00%
Doubtful	12.50% to 70.00%
Loss	25.00% to 100.00%

In addition to overdue basis, Loan and advances have to be classified as Loss on the basis of other factors like CIB blacklisting, collateral value, misuse of fund, bankruptcy of the borrower etc. the loan falling under pass category is termed as performing loan and the loan falling under remaining three categories is termed as non-performing loan. The LLP set aside for performing loan is defined as General Loan Provision (GLLP) and LLP aside for non-performing loan is defined as Specific Loan Loss Provision (SLLP). Besides this, if a bank provides any provision in excess of the proportion as required under the directives of NRB, the whole amount of such additional provision may be included in GLLP.

The new directive issued in 2001, regarding loan classification and provisioning was effective from the fiscal year 2001/02. Here the five year data regarding loan classification and provisioning of two banks as per new directive has been analyzed as follows.

Table 4.14

Loan Classification and Provisioning of NIBL & HBL as per FY 2006/07

(Rs. In Million)

S. N.	Particular	NIBL				HBL			
		Loan & Adv.	% of Total loan	LLP	% of Total LLP	Loan & Adv.	% of Total loan	LLP	% of Total LLP
1	**Performing Loan**	**17347**	**97.63**	**178**	**36.92**	**17152**	**96.39**	**307**	**38.62**
1.1	Pass Loan	17310	97.41	173	35.94	16698	93.84	167	21.02
1.2	Restructured	38	0.21	5	0.97	454	2.55	140	17.60
2	**Non-Performing Loan**	**422**	**2.37**	**304**	**63.08**	**642**	**3.61**	**488**	**61.38**
2.1	Substandard	97	0.55	25	5.09	72	0.41	18	2.31
2.2	Doubtful	86	0.48	43	8.93	195	1.10	97	12.25
2.3	Loss	239	1.35	237	49.07	375	2.11	373	46.82
Total		**17769**	**100.00**	**483**	**100.00**	**17794**	**100.00**	**796**	**100.00**

The table no.4.14 shows different categories of loan and advances and loan loss provision provided to each category of loan and advances of NIBL and HBL for the fiscal year 2006/07. The total loan outstanding of NIBL was Rs. 17,769 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 97.63%, 0.55%, 0.48% and 1.35% respectively. Out of performing loan pass loan compromises 97.41% and restructured loan is 0.21%. Hence it is clear that 97.63% of total loan and remaining 2.37% is non-performing loan. Similarly out of total provision provided of Rs. 483 million, 36.92% comprises for performing loan and the provision provided for substandard, doubtful and loss loan comprises 5.09%, 8.93% and 49.07% respectively making provision for non-performing loan 63.08% of total LLP. Hence it can be understood that the General LLP comprises 36.92% and Specific LLP comprises 63.08% of total LLP.

Similarly, the total loan and advances of HBL in 2006/07 was Rs. 17,794 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 96.39%, 0.41%, 1.10% and 2.11% respectively. Out of performing loan pass loan compromises 93.84% and restructured loan is 2.55%. Out of total provision provided of Rs. 796 million, the respective percentage of performing loan, SS, DF and loss loan is 38.62%, 2.31%, 12.25% and 46.82%. Hence it can be understood that the General LLP comprises 38.62% and specific LLP comprises remaining 61.38%. Following figure no. 4.11 and 4.12 shows the loan categorization of NIBL and HBL of fiscal year 2006/07.

Figure 4.11

Loan Categorization of NIBL as per FY 2006/07

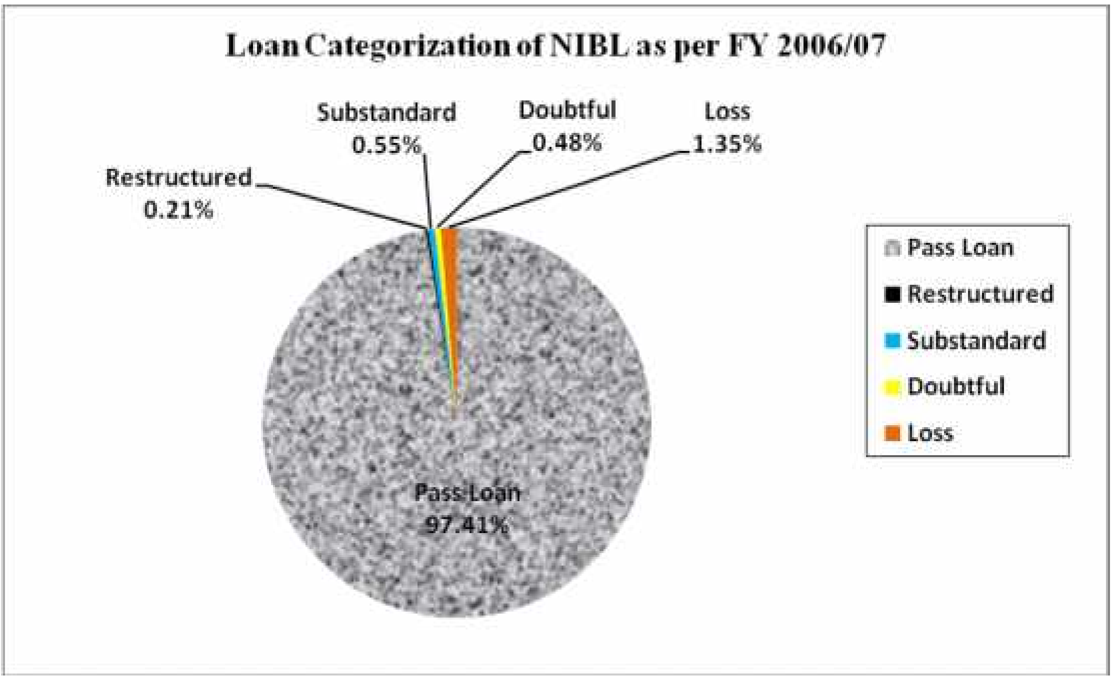


Figure 4.12

Loan Categorization of HBL as per FY 2006/07

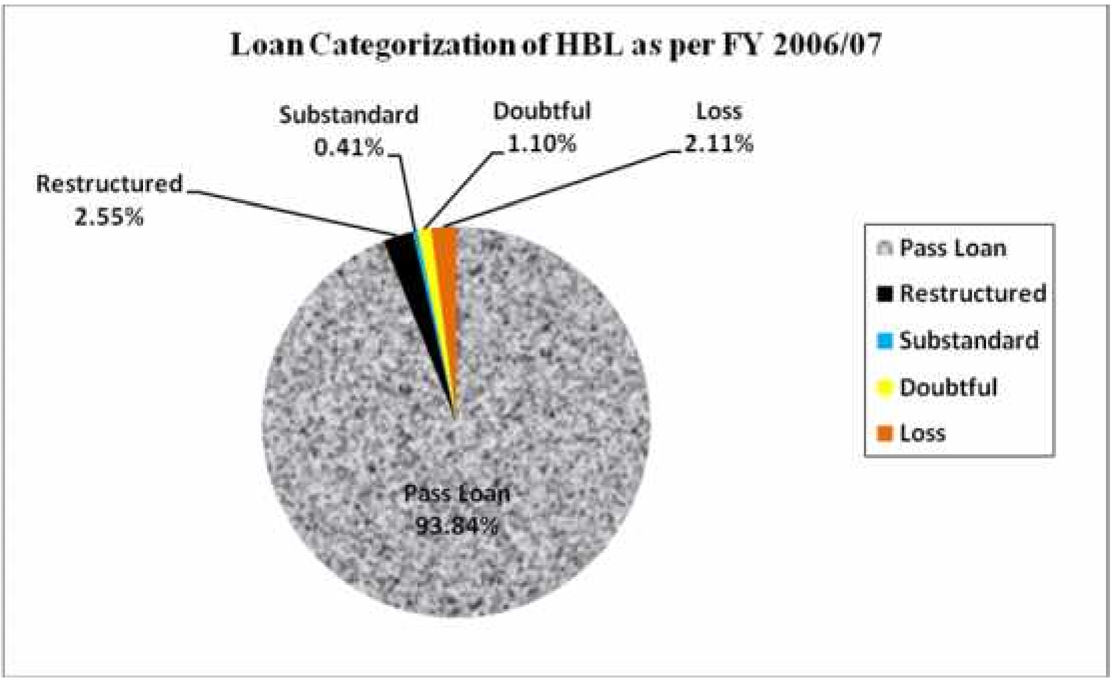


Table 4.15

Loan Classification and Provisioning of NIBL & HBL as per FY 2007/08

(Rs. in Million)

S. N.	Particular	NIBL				HBL			
		Loan & Adv.	% of Total loan	LLP	% of Total LLP	Loan & Adv.	% of Total loan	LLP	% of Total LLP
1	**Performing Loan**	**27220**	**98.88**	**280**	**52.53**	**19702**	**97.64**	**353**	**51.70**
1.1	Pass Loan	27177	98.72	274	51.53	19358	95.93	196	28.81
1.2	Restructured	43	0.16	5	1.01	345	1.71	156	22.89

2	**Non-Performing Loan**	**309**	**1.12**	**253**	**47.47**	**477**	**2.36**	**329**	**48.30**
2.1	Substandard	62	0.22	15	2.90	54	0.27	13	1.98
2.2	Doubtful	21	0.08	10	1.95	214	1.06	107	15.72
2.3	Loss	227	0.82	227	42.62	209	1.03	209	30.60
Total		**27529**	**100.00**	**533**	**100.00**	**20180**	**100.00**	**682**	**100.00**

The table no.4.15 shows different categories of loan and advances and the provision provided to each category of loan and advances of NIBL and HBL for the fiscal year 2007/08. The total loan outstanding of NIBL was Rs. 27,529 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 98.88%, 0.22%, 0.08% and 0.82% respectively. Out of performing loan pass loan compromises 98.72% and restructured loan is 0.16%. Hence it is clear that 98.88% of total loan is performing loan and remaining 1.12% is non-performing loan. Similarly out of total provision provided of Rs. 533 million, 52.53% comprises for performing loan and the provision provided for substandard, doubtful and loss loan comprises 2.90%, 1.95% and 42.62% respectively making provision for non-performing loan 47.47% of total LLP. Hence it can be understood that the general LLP comprises 52.53% and specific LLP comprises 47.47% of total LLP.

Similarly, the total loan outstanding of HBL in 2007/08 was Rs. 20,180 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 97.64%, 0.27 %, 1.06% and 1.03% respectively. Out of performing loan pass loan compromises 95.93% and restructured loan is 1.71%. Out of total provision provided of Rs. 682 million, the respective % of performing loan, SS, DF and loss loan is 51.70, 1.98%, 15.72%, and 30.60%. Hence it can be understood that the General LLP comprises 51.70% and specific LLP comprises remaining 48.30%. Following figure no. 4.13 and 4.14 shows the loan categorization of NIBL and HBL of fiscal year 2007/08.

Figure 4.13

Loan Categorization of NIBL as per FY 2007/08

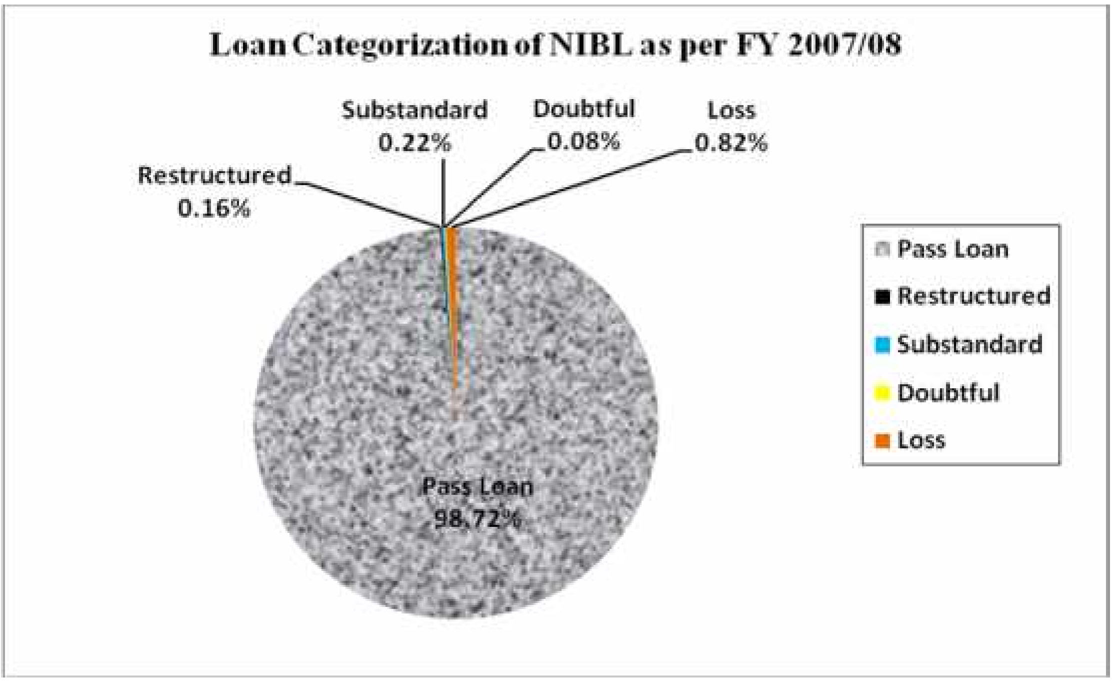


Figure 4.14

Loan Categorization of HBL as per FY 2007/08

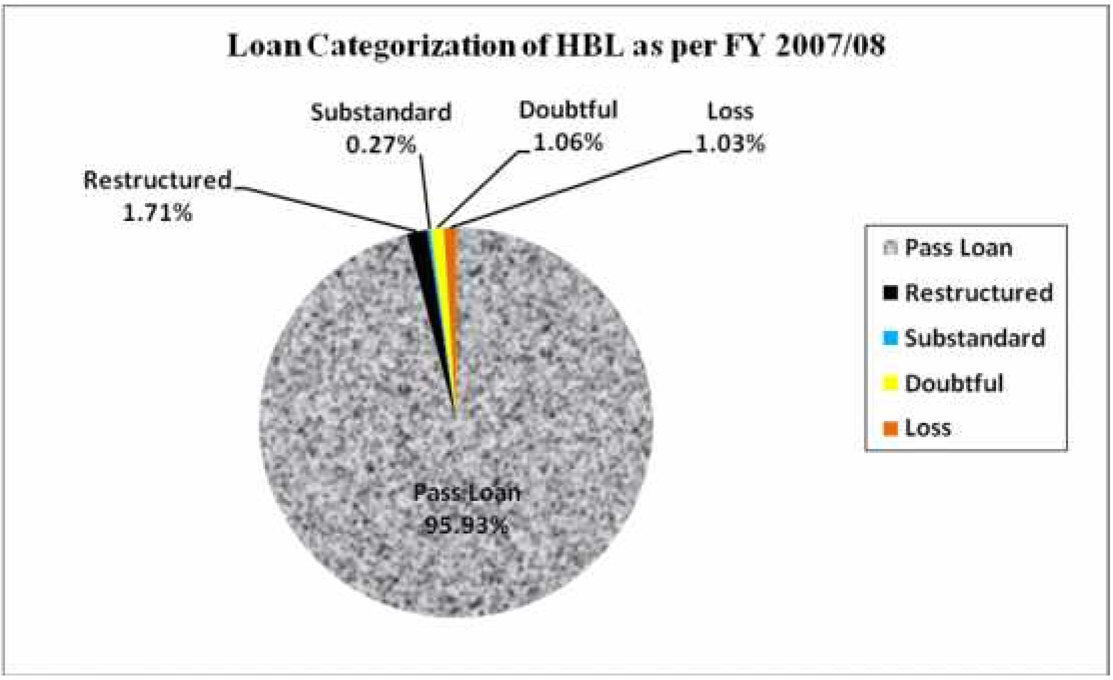


Table 4.16

Loan Classification and Provisioning of NIBL & HBL as per FY 2008/09

(Rs. in Million)

S. N.	Particular	NIBL				HBL			
		Loan & Adv.	% of Total loan	LLP	% of Total LLP	Loan & Adv.	% of Total loan	LLP	% of Total LLP
1	**Performing Loan**	**36613**	**99.42**	**386**	**65.85**	**24968**	**97.84**	**365**	**50.29**
1.1	Pass Loan	36576	99.32	381	65.06	24667	96.66	248	34.10
1.2	Restructured	37	0.10	5	0.80	302	1.18	118	16.19
2	**Non-Performing Loan**	**214**	**0.58**	**200**	**34.15**	**551**	**2.16**	**361**	**49.71**
2.1	Substandard	11	0.03	3	0.46	168	0.66	74	10.21
2.2	Doubtful	11	0.03	6	0.98	195	0.76	99	13.63
2.3	Loss	192	0.52	192	32.71	189	0.74	188	25.87
Total		**36827**	**100.00**	**586**	**100.00**	**25520**	**100.00**	**726**	**100.00**

The table no.4.16 shows different categories of loan and advances and the provision provided to each category of loan and advances of NIBL and HBL for the fiscal year 2008/09. The total loan outstanding of NIBL was Rs. 36,827 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 99.42%, 0.03%, 0.03% and 0.52% respectively. Out of performing loan pass loan compromises 99.32% and restructured loan is 0.10%. Hence it is clear that 99.42% of total loan is performing loan and remaining 0.58% is non-performing loan. Similarly out of total provision provided of Rs. 586 million, 65.85% comprises for performing loan and the provision provided for substandard, doubtful and loss loan comprises 0.46%, 0.98% and 32.71% respectively making provision for non-performing loan 34.15% of total LLP. Hence it can be understood that the General LLP comprises 65.85% and Specific LLP comprises 34.15% of total LLP.

Similarly, the total loan outstanding of HBL in 2008/09 was Rs. 25,520 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 97.84%, 0.66 %, 0.76% and 0.74% respectively. Out of performing loan pass loan compromises 96.66% and restructured loan is 1.18%. Out of total provision provided of Rs. 726 million, the respective % of performing loan, SS, DF and loss loan is 50.29, 10.21%, 13.63%, and 25.87%. Hence it can be understood that the General LLP comprises 50.29% and specific LLP comprises remaining 49.71%. Following figure no. 4.15 and 4.16 shows the loan categorization of NIBL and HBL of fiscal year 2008/09.

Figure 4.15

Loan Categorization of NIBL as per FY 2008/09

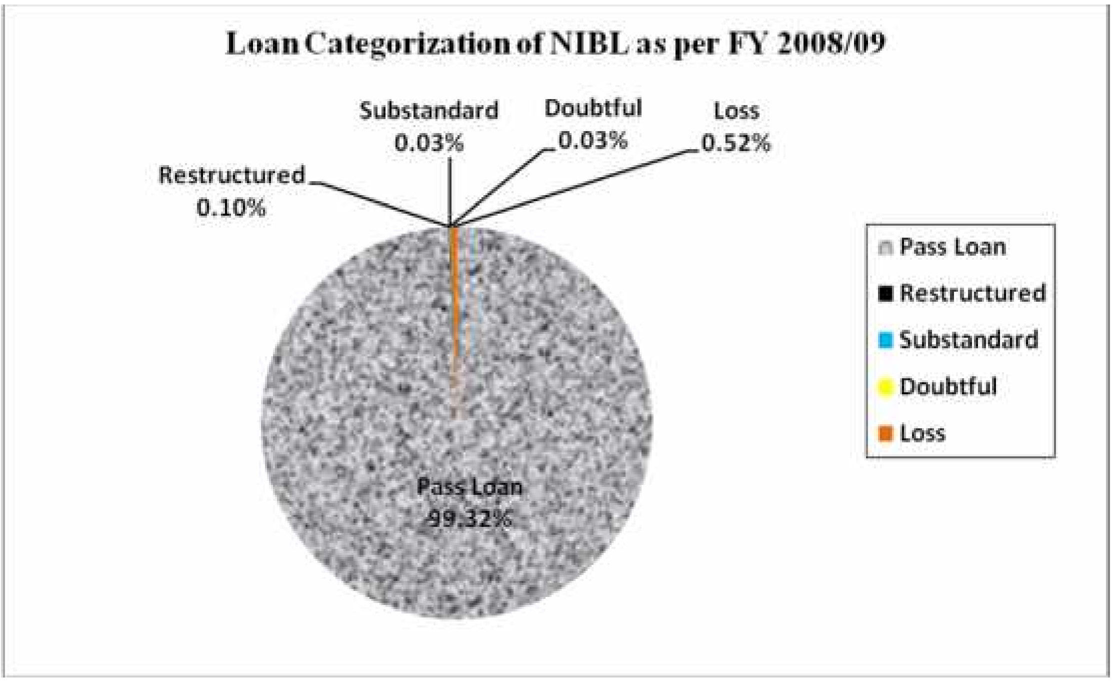


Figure 4.16

Loan Categorization of HBL as per FY 2008/09

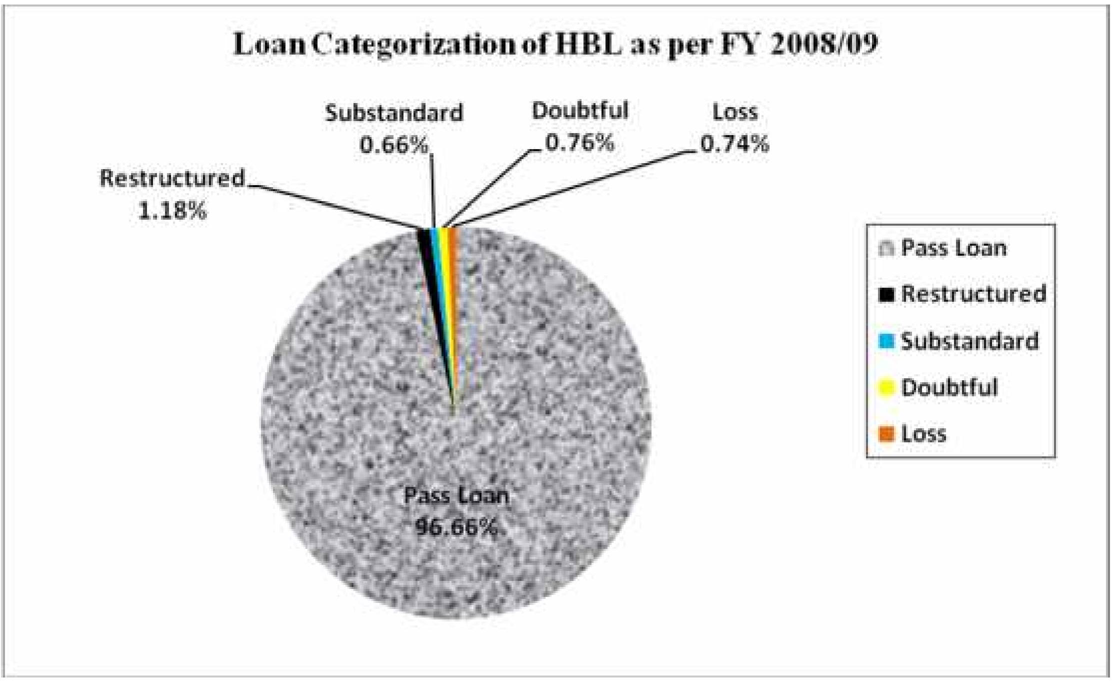


Table 4.17

Loan Classification and Provisioning of NIBL & HBL as per FY 2009/10

(Rs. in Million)

S. N.	Particular	NIBL				HBL			
		Loan & Adv.	% of Total loan	LLP	% of Total LLP	Loan & Adv.	% of Total loan	LLP	% of Total LLP
1	**Performing Loan**	**40694**	**99.38**	**423**	**67.19**	**28099**	**96.48**	**305**	**26.72**
1.1	Pass Loan	40674	99.33	421	66.79	27916	95.85	282	24.71
1.2	Restructured	20	0.05	3	0.40	183	0.63	23	2.00

2	**Non-Performing Loan**	**254**	**0.62**	**207**	**32.81**	**1025**	**3.52**	**838**	**73.28**
2.1	Substandard	56	0.14	14	2.21	123	0.42	47	4.10
2.2	Doubtful	11	0.03	6	0.87	221	0.76	110	9.65
2.3	Loss	187	0.46	187	29.73	682	2.34	681	59.54
Total		**40948**	**100.00**	**630**	**100.00**	**29124**	**100.00**	**1143**	**100.00**

The table no. 4.17 shows different categories of loan and advances and the provision provided to each category of Loan and advances of NIBL and HBL for the fiscal year 2009/10. The total loan outstanding of NIBL was Rs. 40,948 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 99.38%, 0.14%, 0.03% and 0.46% respectively. Out of performing loan pass loan compromises 99.33% and restructured loan is 0.05%. Hence it is clear that 99.38% of total loan is performing loan and remaining 0.62% is non-performing loan. The loan loss provision provided is Rs. 630 million. Out of the total provision provided, 67.19% comprises for performing loan and the provision provided for substandard, doubtful and loss loan comprises 2.21%, 0.87% and 29.73% respectively making provision for non-performing loan 67.19% of total LLP. Hence it can be understood that the General LLP comprises 67.19% and Specific LLP comprises 32.81% of total LLP.

Similarly, the total loan outstanding in 2009/10 of HBL was Rs. 29,124 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 96.48%, 0.42 %, 0.76% and 2.34% respectively. Out of performing loan pass loan compromises 95.85% and restructured loan is 0.63%. Out of total provision provided of Rs. 1143 million, the respective % of performing loan, SS, DF and loss loan is 26.72%, 4.10%, 9.65% and 59.54%. Hence it can be understood that the General LLP comprises 26.72% and specific LLP comprises remaining 73.28%. Following figure no. 4.17 and 4.18 shows the loan categorization of NIBL and HBL of fiscal year 2009/10.

Figure 4.17

Loan Categorization of NIBL as per FY 2009/10

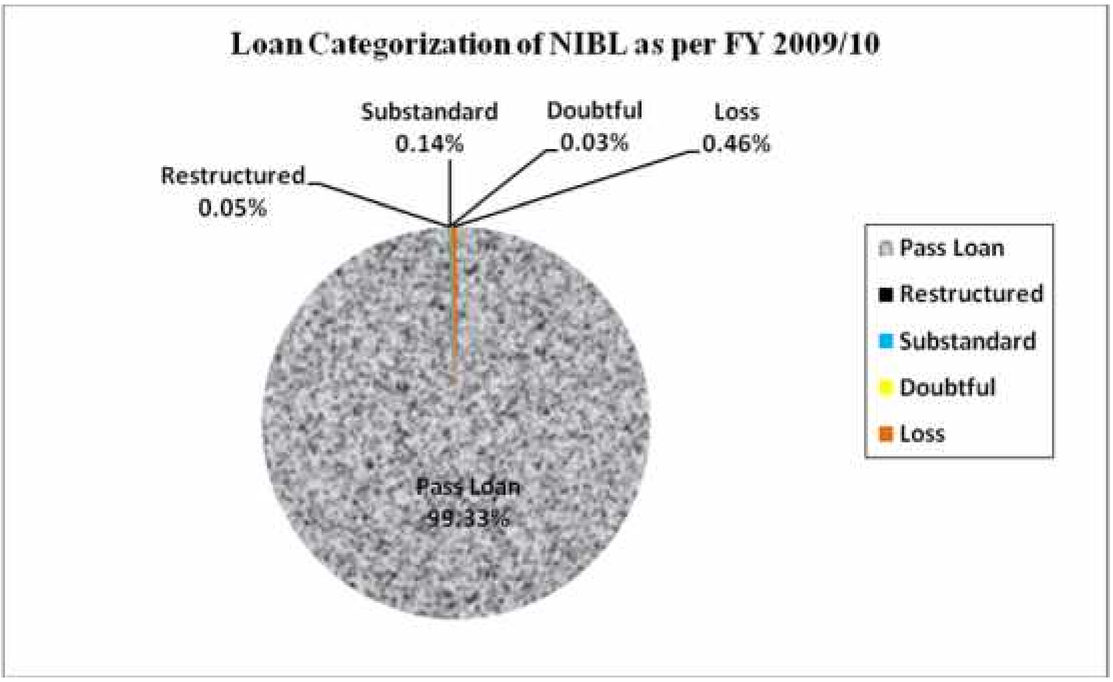


Figure 4.18

Loan Categorization of HBL as per FY 2009/10

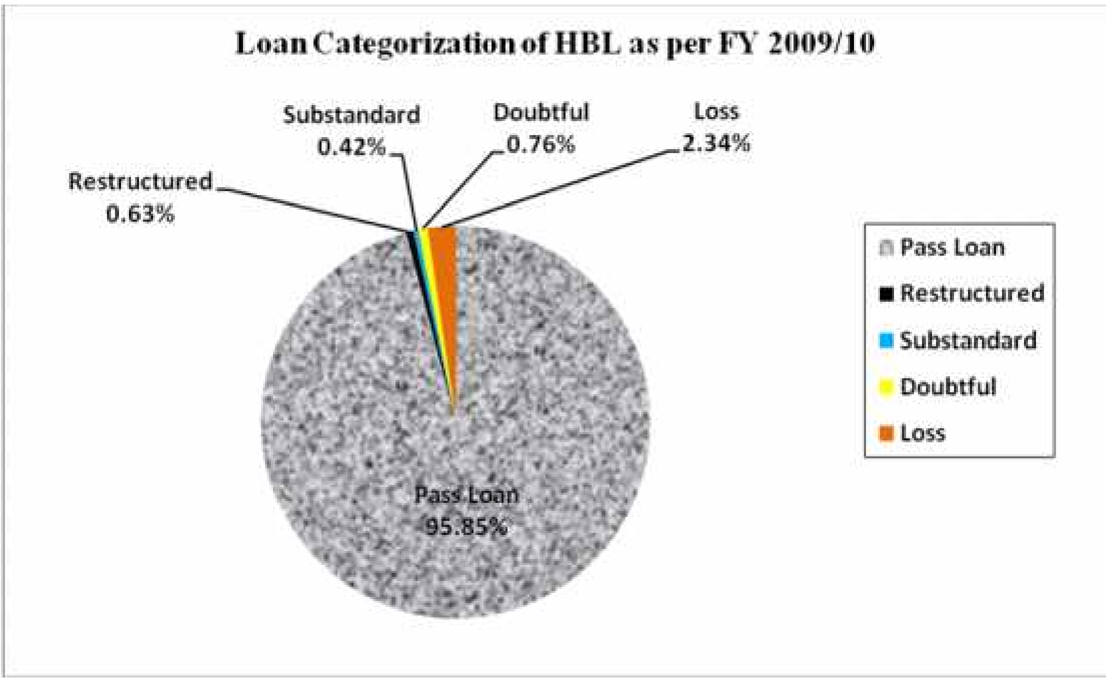


Table 4.18

Loan Classification and Provisioning of NIBL & HBL as per FY 2010/11

(Rs. in Million)

S. N.	Particular	NIBL				HBL			
		Loan & Adv.	% of Total loan	LLP	% of Total LLP	Loan & Adv.	% of Total loan	LLP	% of Total LLP
1	**Performing Loan**	**41492**	**99.06**	**416**	**52.52**	**31765**	**96.35**	**397**	**28.31**
1.1	Pass Loan	41492	99.06	416	52.52	31577	95.78	318	22.70
1.2	Restructured	-	0.00	-	0.00	188	0.57	79	5.61
2	**Non-Performing Loan**	**395**	**0.94**	**376**	**47.48**	**1203**	**3.65**	**1005**	**71.69**
2.1	Substandard	23	0.05	6	0.72	216	0.66	54	3.86
2.2	Doubtful	4	0.01	2	0.26	73	0.22	37	2.62
2.3	Loss	368	0.88	368	46.50	914	2.77	914	65.21
Total		**41888**	**100.00**	**792**	**100.00**	**32968**	**100.00**	**1401**	**100.00**

The table no.4.18 shows different categories of loan and advances and the provision provided to each category of loan and advances of NIBL and HBL for the fiscal year 2010/11. The total loan outstanding of NIBL was Rs. 41,888 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 99.06%, 0.05%, 0.01% and 0.88% respectively. Hence it is clear that 99.06% of total loan is performing loan and remaining 0.94% is non-performing loan. The loan loss provision provided for the year 2010/11 is Rs. 792 million. Out of the total provision provided, 52.52% comprises for performing loan and the provision provided for substandard, doubtful and loss loan comprises 0.72%, 0.26% and 46.50% respectively making provision for non-performing loan 47.48% of total LLP. Hence it can be understood that the General LLP comprises 52.52% and Specific LLP comprises 47.48% of total LLP.

Similarly, the total loan outstanding of HBL in 2010/11 was Rs. 32,968 million. Out of the total loan, performing loan, substandard, doubtful and loss loan comprises 96.35%, 0.66 %, 0.22% and 2.77% respectively. Out of performing loan pass loan compromises 95.78% and restructured loan is 0.57%. Out of total provision provided of Rs. 1401 million, the respective % of Pass, SS, DF and Loss loan is 28.31%, 3.86%, 2.62% and 65.21%. Hence it can be understood that the General LLP comprises 28.31% and specific LLP comprises remaining 65.21%. Following figure no. 4.19 and 4.20 shows the loan categorization of NIBL and HBL of fiscal year 2010/11.

Figure 4.19

Loan Categorization of NIBL as per FY 2010/11

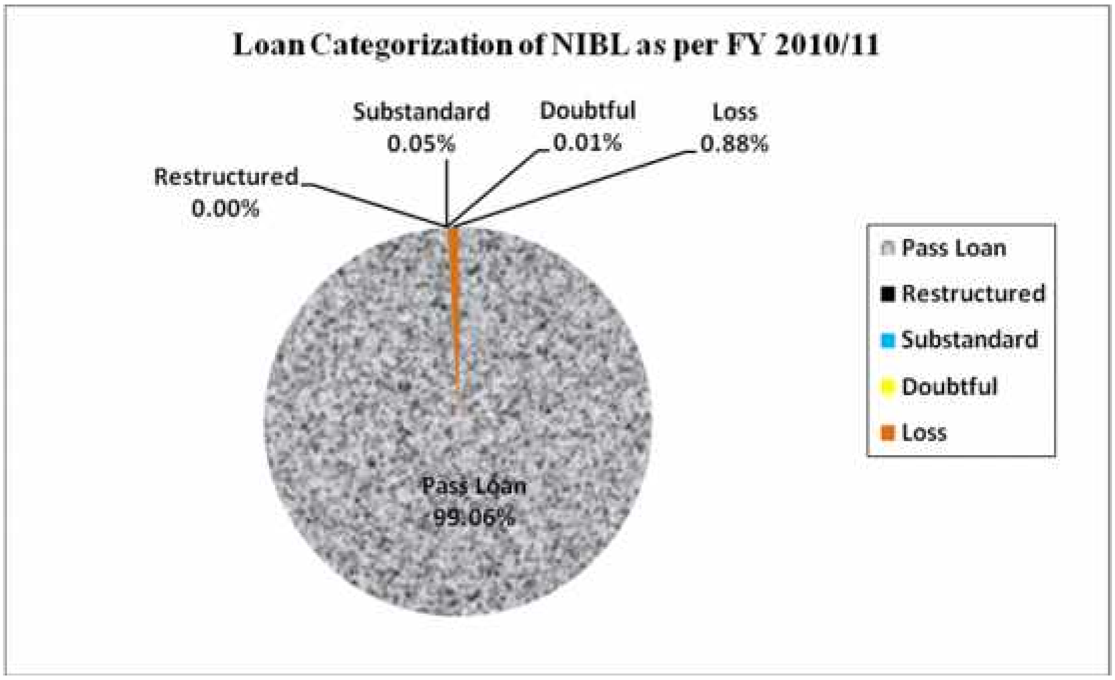
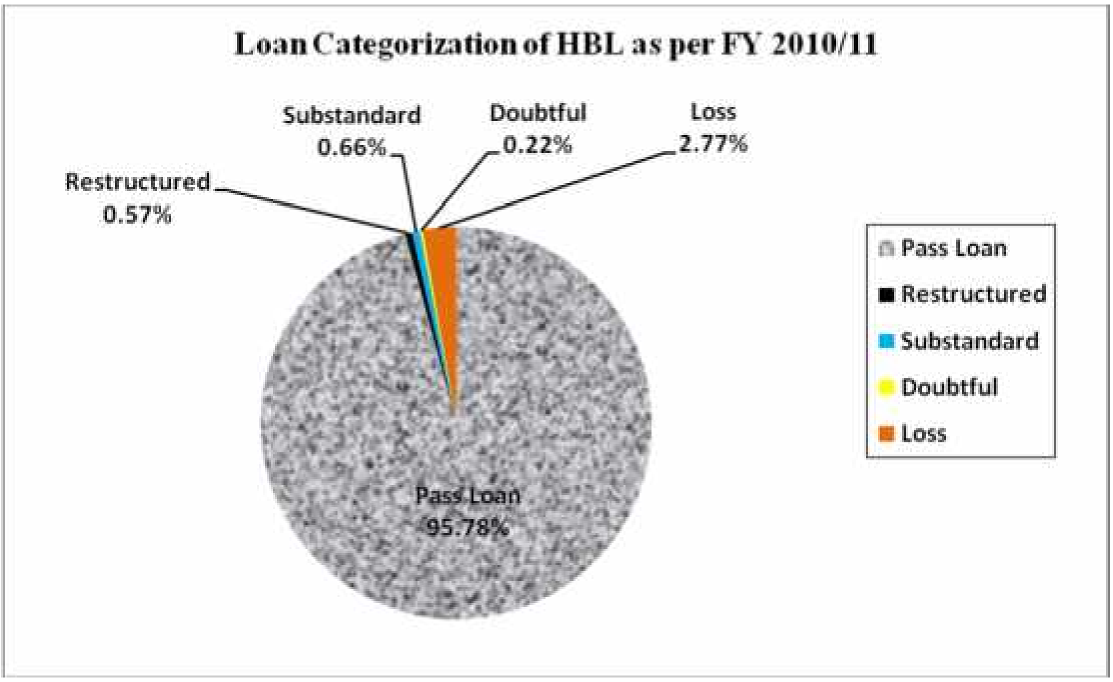


Figure 4.20

Loan Categorization of HBL as per FY 2010/11



Effects on Profitability

Latest Loan Loss Provision norm have a great impact on profitability of the banks. As earlier mentioned, Loan Loss Provision is deducted form the profit of the bank. Therefore the net profit of the bank will come down by the amount of provision. Hence increase in LLP means lesser net profit resulting to less Earning per Share (EPS), less Dividend per Share (DPS) or no dividend at all and finally lower Market Value per Share (MVPS). If any banks make profit less than the amount of provision to be made, it may have to show losses in the balance sheet. For instance the LLP of NIBL and HBL as on mid July 2011 is Rs. 792 million and Rs 1401 million respectively. Hence the net profit of NIBL and HBL is reduced by the respective provisioned amount.

However, the impact of loan of Loan Loss Provision on profitability of banks is of short term. After few years, when banks have enough provision for loss Loan & have sound credit management, the profitability will again pick up. Hence in long term basis banks will enjoy greater cushion against loan disbursed and improve their financial strength leading to increased profitability.

4.5 Study of Response of Officials of NIBL and HBL

Regarding the impact of non-performing assets a questionnaire was developed as shown in Appendix H. A total number of twelve officials of NIBL and HBL participated in the quarries.

The questionnaire revealed opinions of the bank officials towards the non-performing assets. All the officials agreed that the directives related to loan classification and provisioning for a commercial bank is very important. Most of the respondents answered that present directives related to loan classification and provisioning is appropriate and better than the previous one. Similarly, all participants agreed that will increase provision for loan loss by the new directives on provision for loan loss of commercial banks.

However, in some questions the officials found to be disagreeable. Out of twelve, seven respondents answered that affected to lesser dividend by the present loan classification and provisioning directives and rest five respondents said that EPS decreased. As well as, the banks cope with the problem brought about by this amendment of loan classification and provisioning directives will control the credit disbursal by being more stringent, eight respondents said and four respondents said that will strengthen the monitoring and follow up procedures. All respondents are agreed to banking industry is effected by the problem of NPA. Most of officials are said that the setting up recovery cell for resolve the problem of NPA and only two officials select that for it will solve by hiring Asset Management Company (AMC).

Officials are divided to the major factors for increasing NPA; three respondents said that it is increasing by improper credit appraisal system. Similarly, five respondents agreed that by economic slowdown, three respondents said that by ineffective credit monitoring and supervision system and two respondents said that political pressure to lend to un-creditworthy borrower.

4.5 Major Findings of the Study

From the analysis of data, following major findings have been obtained.

The average Loan and advances to total asset ratio of NIBL and HBL during the study period is found to be 69.59% and 61.91% respectively. The relatively low ratio of HBL is the indication of risk adverse attitude of the management or they have the policy of investing low in the risky assets i.e. Loan and advances. HBL has higher proportion of its investment in risk free or nominally risky asset like treasury bills; National saving bonds etc. here the ratio is the highest of NIBL but issued Loan and advances are not generating the desired income. HBL shows the highest degree of deviation and variation while NIBL has the most consistent ratio throughout the study period.

The core banking function is to be mobilize the funds obtained from the depositors and how successfully this function have been discharged by the banks is measured by the ratio of Loan and advances to total deposit ratio or simply CD ratio. The average CD ratio of NIBL and HBL during the study period is to be 79.32% and 70.83% respectively. Even though this ratio is the highest of NIBL, it has the most consistent and least deviated ratio during the study period where as HBL has higher deviation and variability in this ratio.

The analysis of non-performing Loan to total Loan revealed that average NPL of NIBL and HBL is 1.14% and 3.30% of total loan respectively. That means 98.86% and 96.70% of total loan of NIBL and HBL is performing loan. Hence HBL has significantly higher proportion of the non-performing loan in the total Loan portfolio in the beginning of the study period but decreasing significantly in next 2 years but also increasing then. It shows that trying the result of the banks effective credit management and its efforts of recovering bad debts through establishment of recovery cell. During the study period this ratio is the least in NIBL but this ratio decreasing trend in first 3 years and then it increasing by low proportion. HBL has highest deviation and the least variation and NIBL has lowest deviation and the highest variation in this ratio through out the study period.

Loan loss provision ratio of NIBL and HBL are 1.93% and 3.77% respectively. Since higher ratio is an indication of higher non-performing loan in the total Loan and advances HBL's relatively higher ratio is the result of the higher proportion of NPL in the total loan. In comparison, NIBL shows decreasing trend but slightly increase in last period of study period, in this ratio which means NIBL's asset quality is improving. Similarly, HBL shows also decreasing first three years but then it is increasing trend. HBL has the highest deviation and lowest variation of the ratio as per comparison of NIBL.

The average ratio of provision held to non-performing loan of NIBL and HBL was to be 198.11% and 118.80% respectively. Hence NIBL has significantly higher ratio in comparison to HBL, which portrays that the bank has adequate provision against non-performing loan. Even though HBL has the provided required provision on each category of NPL as per NRB directives, it has not enough provision against NPL if all the NPL goes in default. NIBL shows the highest deviation and highest variability in this ratio than the HBL.

The main objective of commercial banks is to earn profit through mobilization of fund. The ratio of returns on Loan and advances ratio revealed that NIBL and HBL's return on loan and advances are 2.74% and 2.66%. The NIBL is able to generate the adequate profit than HBL investing in risky asset. HBL has the highest variably than NIBL.

The correlation coefficient between LLP and Loan and advances of NIBL and HBL is 0.8345 and 0.8605. Here correlation coefficient of NIBL and HBL are more than their value of 6 times P.E., it is significant and reliable. So it can be interpreted that there is high degree of positive correlation between LLP and loan and advances of NIBL and HBL.

The correlation between LLP and NPL revealed that there is positive correlation between LLP and NPL. As earlier mentioned higher provision needs to be provided for NPL, higher would be the LLP. The correlation coefficient between these two variables in NIBL and HBL are 0.0800 and 0.9900. The correlation coefficient of NIBL is insignificant and there is no evidence of correlation because the correlation coefficient is less than its 6 times P.E. but that of HBL is significant and reliable.

While analyzing correlation between Loan and advances and deposit, it has been found that NIBL and HBL have high degree of positive correlation between these two variables. The respective correlation coefficient of NIBL and HBL is 0.9972 and 0.9954 respectively, which is significant and reliable because it is more than its 6 times P.E.

Trend analysis was done based on the data of past five years and forecast was made for next five years. The trend of Loan and advances showed and increasing trend in regards to NIBL and HBL but rate of increment NIBL is higher than that of HBL. The Loan and advances of NIBL increasing at the rate of Rs. 6,165.63 million every year and HBL is increasing at the rate of Rs. 3,929.32 million every year.

From the trend analysis of NPL, it is found that NPL is decreasing in case of NIBL and in case of HBL it is increasing. The NPL of NIBL is decreasing at the rate of Rs. 8.85 million every year and that of HBL is increasing at the rate of Rs. 223.12 million every year. The decreasing trend of NPL in NIBL is due to its efforts towards recovering bad debts.

From the trend analysis of LLP, it is found that LLP is expected to increase in coming year in two banks. The LLP of NIBL is increasing Rs. 71.65 million every year while the LLP of NIBL is increasing by Rs. 167.22 million. The low rate LLP of NIBL shows that NIBL is successful to control to increase non-performing loan than HBL.

From the trend analysis of net profit, it is found that net profit is expected to increase in coming year in two banks. The net profit of NIBL is increasing Rs. 191.97 million every year while the net profit of HBL is increasing by Rs. 67.55 million. The high rate of net profit earning of NIBL is due to more investment in less risky asset resulting low NPL and hence less loan loss provision.

As per the latest directive, Loan and advances are to be classified into four categories, namely Pass, Substandard, Doubtful and Loss with respective provisioning 1%, 25%, 50% and 100% on the basis of aging of past dues. Besides this in case of insured priority and deprived sector loan, the provisioning requirement is one-fourth of that of normal loan loss provisioning requirement. Hence the respective provisioning requirement for Pass, Substandard, Doubtful and Loss Loan are 0.25%, 6.25%, 12.5%

and 25% of the outstanding loan. In case of rescheduled or restructured or swapped loan, if such loans fall under pass category, the minimum provisioning requirement is 12.5% and if this is the base of priority sector loan, 3.125% provisioning should be provided for the probable loss. Further if the loan is granted only against personal guarantee, the provisioning required for Pass, Substandard and Doubtful is 21%, 45% and 70% respectively.

It is observed that officials of both banks think directives related to loan classification and provisioning is very important and more appropriate than previous one. The officials of both banks feel that new directives on provision for loan loss will increase provision for loan loss and it affected to lesser dividend and decrease EPS. The banks cope with the problem brought about by this amendment of loan classification and provisioning will control the credit disbursal by being more stringent and some of them say will strengthen the monitoring and follow up procedures. All officials of both banks feel that banking industry is effected by the problem of NPA and its resolve by setting up recovery cell and some of them said that hiring Asset Management Company (AMC). Economic slowdown/recession is the major factors to increasing NPA and then ineffective credit monitoring and supervision system and then improper credit appraisal system and also political pressure to lend to un-creditworthy borrowers.

CHAPTER – FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

Finally this chapter includes the summary, conclusions and recommendations based on the result of the analysis of the data.

5.1 Summary

Bank plays an important role in the economic development of the country of the country as the issue of development always rests upon the mobilization of resources. Banks deals in the process of channelizing the available resources to the needy sector causing overall economic development. This research is aimed at studying the non-performing loan and loan loss provisioning of commercial banks. For this purpose, descriptive cum analytical research design was adopted. Out of the total population of 32 commercial banks, two banks were taken as sample using Judgmental Sampling Method. Two major joint venture banks, Nepal Investment Bank Limited and Himalayan Bank Limited were selected from private sector banks. Both primary and secondary data have been used in the study. Primary data has been collected through questionnaire, direct interviews & telephonic interviews and annual reports and other publication forms the basis of secondary data. The data collected from various sources are recorded systematically and presented in appropriate forms of tables and charts and appropriate mathematical, statistical, financial, graphical tools have been applied to analyze the data. The data of five consecutive years of the two selected banks have been analyzed to meet the objective of the study.

NIBL have the highest proportion of the loans and advances in the total asset structure but HBL has relatively lower loans and advances in the total asset structure. The credit deposit ratio also shows the same thing. It indicates the risk adverse attitude of the management of HBL. Regarding NPL and LLP, NIBL has the least NPL and accordingly the least LLP than the HBL. The less orientation towards lending has made this bank successful in to have low ratio of provisioning and lower ratio of non-performing loans. HBL has higher proportion of NPL. The ratio of provision held to NPL of HBL is the highest than NIBL.

Even though, NIBL has higher proportion of investment in loans and advances in comparison to HBL, its return on loans and advances is also comparatively higher than HBL.

There is positive correlation between LLP and loans and advances in NIBL and HBL. This is due to increment of non-performing loan. Amount to be provisioned depends upon the non-performing loan and its quality. Higher provision has to be provided for NPL. Hence even though loans and advance do not increase, if in the same loan portfolio NPL increase, LLP will increase. This has also been shown by the positive correlation between LLP and NPL in the two banks. NIBL and HBL have shown

The trend analysis of loans and advances shows increasing trend in NIBL and HBL. The trend analysis of non-performing loan in NIBL shows decreasing trend in coming years but the trend of LLP is increasing in NIBL. This is due to NIBL's recovery efforts towards reducing NPL through establishment of recovery cell. In case of HBL two NPL and LLP is in increasing trend. The past trend of net profit of both banks exhibit increasing trend in coming years.

As per the least loan classification and provisioning directives loans and advances have to be categorized into four types namely Pass, Substandard, Doubtful and Loss with respective provisioning of 1%, 25%, 50% and 100%. The loan falling under Pass category is regarded as performing loan and that which falls under remaining three categories is regarded as non-performing loan. HBL has higher proportion of loss loan in the total non-performing loan followed by Substandard and doubtful.

Today's banking industry is severely affected by the problem of NPA. Improper credit appraisal system, ineffective credit monitoring & supervision system, economic slowdown, borrower's misconduct, and overvaluation of collateral, political pressure lend to un-creditworthy parties etc. are the major factors leading to non-performing assets. Setting up recovery cell, hiring Asset Management Company etc. are some to the measures to resolve the problem of NPA. Loan classification and loan loss provision also helps to confront the problems thus created due to non performing loans. The latest directives regarding loan classification and loan provisioning is very important for maintaining sound financial health of the banks. the new provisioning directives leads to increment in provision amount of the banks leading to decrement in profitability of the bank but this is only for a short run.

The thesis also studies the responses of 12 bank officials has also been done through research interview.

5.2 Conclusions

Liberalization of financial sector started in 1980s with the aim to streamline it. After that the financial sector widened with more banks and financial institutions. Regarding banking sector there are 32 commercial banks. Even the financial sector developed rapidly in quantity, but in terms of quality it is far behind the developed countries. Bank came into existence mainly with the objectives of collecting idle funds, mobilizing them into productive sector and causing an overall economic development. The banker's have the responsibility of safeguarding the interest of the depositors, the shareholders and the society they are serving. Lending is the major function of any commercial bank and it is the most income generating asset of any commercial bank but there is risk inherent in bank's lending portfolio. In order to cover the risk inherent in the lending portfolio, banks have to make loan loss provision by categorizing the loans into different category as per the NRB directives. Increasing non performing loan is the serious problem of the banking sector in Nepal. Non-performing asset debar the income flow of the bank while claiming additional resources in the form of provisioning and hinder further gainful investments.

It has been found that HBL has very high portion of non-performing loan resulting to higher provision. Hence even the bank has the highest investment in the most income generating asset i.e. loans and advances, it is in loss. Among the two banks NIBL has the least non performing loan and thus the least loan loss provision. In the study period, NPL of both banks decreasing in 2nd period but then it is increasing. It is also a head in generating income. From these indicators it can be said that NIBL is the best among the two banks. in conclusion it can be said that ineffective credit policy, political pressure to lend in un-creditworthy borrowers, overvaluation of collateral are the major causes of mounting non-performing assets. Other factors leading to accumulation of NPAs are weak loan sanctioning process, ineffective credit monitoring and supervision system, economic slowdown, borrower' misconduct etc. continual review and classification of loans enables banks to monitor quality of their loan portfolios and to take remedial action to counter deterioration in credit quality. In addition to this establishing recovery cell, hiring Asset Management Company are also measures to resolve the problem of NPL. The present loan classification and provisioning directive seems more stringent than previous one. As a result more provision has to be apportioned leading to lesser profitability but this kind of negative impact is only for short period. Adequate provisioning strengthens the financial health of the banks and makes them able to face any kind of future contingencies.

The research questionnaire revealed that directives related to loan classification and provisioning for a commercial bank is very important and better than previous one. The directives increase provision for loan loss and lesser dividend and also decrease EPS. The banks cope with the problem brought about by this amendment of loan classification and provisioning directives will control the credit disbursal by being more stringent. Banking industry is severely affected by the problems of NPA and it should be resolve by setting up recovery cell. Economic slowdown, ineffective credit monitoring and supervision system, improper credit appraisal system, political pressure to lend to un-creditworthy borrowers are leading to increase NPA.

5.3 Recommendations

The following recommendations are made based on the analysis of non-performing asset NIBL and HBL.

- The increasing trend of non-performing loan and hence loan loss provision of HBL indicates that the bank's credit portfolio needs serious attention. Hence HBL is recommended to take immediate remedial action for recovering bad debts. Hiring Asset Management Company (AMC) is recommended for HBL to resolve the problem of mounting non performing loan.
- HBL's contribution to loan and advances is relatively low as per total deposit. Entire economy is largely dependent upon the proper execution of lending function by commercial banks. Low level of lending means low level of investment resulting to low level of productivity, which may ultimately affect negativity on the national economy. Loan and advances on the other hand it also

helps to upgrade the economic health of the country. Hence, HBL is recommended to increase its investment in productive sector in the form of loan and advances. However commercial banks are lacking appropriate project for investment.

- The main factors which leads to non-performing loan are improper credit appraisal system, ineffective credit monitoring and supervision system etc. besides that negligence in taking information from Credit information Bureau may also lead to bad debts. Hence two banks are recommended to be more cautious and realistic while granting loans and advances. After advancing loans there should be regular supervision and follow up for proper utilization of loan.
- It is recommended for the banks to initiate training and development program for the employees to make them efficient and professional in credit appraisal, monitoring and proper risk management.
- Following the directives of NRB and acting upon it also reduce many of the credit risk. Besides there are penalty implication on non compliance of the directives. Hence all the two banks are recommended to the directives and they are also suggested to come up with a stronger internal audit department to ensure that the directives are properly implemented.
- The ratio of provision held to non-performing loan of HBL is relatively lower in comparison to NIBL. Even though HBL has made provision for each category of loan as per NRB directives; the total provision amount is not enough in case all the non-performing goes on default or the loan has to be written off. Hence HBL is recommended to increase this ratio by reducing non-performing loan.
- The regulation regarding loan classification and provisioning is stringent and tighter than the previous. Hence NRB should not only impose directives but also create supportive environment for the commercial banks. NRB is recommended to strengthen Credit Information Bureau (CIB) so that banks can get required credit information about the borrowers on time. This would help in reducing NPL.
- Both banks recommended consult to the bank officials to decrease problems of NPA. The factors, which lead to increasing NPA should minimize and should manage by proper credit appraisal system and effective credit monitoring and supervision system.

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Appendix - A

FIGURES USED IN THE STUDY

(Rs. in Million)

Total Asset

Banks	Fiscal Year				
	2006/07	2007/08	2008/09	2009/10	2010/11
NIBL	27590.84	38873.31	53010.80	57305.41	58356.83
HBL	33519.14	38175.33	39320.32	42717.12	46736.20

Total Deposit

Banks	Fiscal Year				
	2006/07	2007/08	2008/09	2009/10	2010/11
NIBL	24488.86	34451.73	46698.10	50094.73	50138.12
HBL	30048.42	31842.79	34681.35	37611.20	40920.63

Loan and Advances

Banks	Fiscal Year				
	2006/07	2007/08	2008/09	2009/10	2010/11
NIBL	17769.10	27529.30	36827.16	40948.44	41887.69
HBL	17793.72	20179.61	25519.52	29123.75	32968.27

Non-Performing Loan

Banks	Fiscal Year				
	2006/07	2007/08	2008/09	2009/10	2010/11
NIBL	421.97	309.47	213.91	274.33	395.28
HBL	641.62	477.23	551.31	1208.12	1391.75

Performing Loan

Banks	Fiscal Year				
	2006/07	2007/08	2008/09	2009/10	2010/11
NIBL	17347.12	27219.83	36613.25	40694.41	41492.41
HBL	17152.10	19702.38	24968.21	28098.92	31764.98

Loan Loss Provision

Banks	Fiscal Year				
	2006/07	2007/08	2008/09	2009/10	2010/11
NIBL	482.67	532.65	585.95	630.13	792.18
HBL	795.73	682.09	726.36	1143.13	1401.29

Net Profit

Banks	Fiscal Year				
	2006/07	2007/08	2008/09	2009/10	2010/11
NIBL	501.40	696.73	900.62	1265.95	1176.64
HBL	491.82	635.87	752.83	508.80	893.11

Note:

- The entire figures presented above are rounded off to the nearest Million rupees
- The data presented herein are pertained to mid July of each fiscal year.
- The data presented herein are based on the amount mentioned in the annual reports of respective years.
- Loan and advances also include bill purchased and discounted.

Appendix - B

Calculation of Mean, S.D., C.V. and Loans and Advances to Total Asset Ratio of NIBL (Sample Calculation)

Years (Mid July)	Ratio (X) %	$\left(X - \overline{X}\right)$	$\left(X - \overline{X}\right)^2$
2007	64.40	-5.186	26.8946
2008	70.82	1.234	1.5227
2009	69.47	-0.116	0.0134
2010	71.46	1.874	3.5119
2011	71.78	2.194	4.8136
N=5	$\sum X = 347.93$		$\sum\left(X - \overline{X}\right)^2 = 36.7562$

We have,

Mena (X) = $\frac{\sum X}{N} = \frac{347.93}{5} = 69.586\%$

Standard Deviation (σ) = $\sqrt{\frac{\sum\left(X - \overline{X}\right)^2}{N}} = \sqrt{\frac{36.7562}{5}} = 2.71$

Coefficient of Variation (C.V.) = $\frac{\pm}{\overline{X}} \times 100 = \frac{2.71}{69.586} \times 100 = 3.89\%$

Similarly the Mean, S.D, and C.V. of other ratios of the NIBL have been calculated.

Appendix - C

Calculation of Mean, S.D., C.V. and Loans and Advances to Total Asset Ratio of HBL (Sample Calculation)

Years (Mid July)	Ratio (X) %	$\left(X - \overline{X}\right)$	$\left(X - \overline{X}\right)^2$
2007	53.09	-8.824	77.8630
2008	52.86	-9.054	81.9749
2009	64.90	2.986	8.9162
2010	68.18	6.266	39.2627
2011	70.54	8.626	74.4079
N=5	$\sum X = 309.57$		$\sum\left(X - \overline{X}\right)^2 = 282.4247$

We have,

Mean (X) = $\frac{\sum X}{N} = \frac{309.57}{5} = 61.914\%$

Standard Deviation (σ) = $\sqrt{\frac{\sum\left(X - \overline{X}\right)^2}{N}} = \sqrt{\frac{282.4247}{5}} = 7.52$

Coefficient of Variation (C.V.) = $\frac{\pm}{\overline{X}} \times 100 = \frac{7.52}{61.914} \times 100 = 12.14\%$

Similarly the Mean, S.D, and C.V. of other ratios of the HBL have been calculated.

Appendix - D

Calculation of Correlation Coefficient, P.E. and 6*P.E. of NIBL (Sample Calculation)

(Rs. in Million)

Year (Mid July)	Loan and Advances (X)	LLP (Y)	$x = X - \overline{X}$	$y = Y - \overline{Y}$	x^2	y^2	$x \times y$
2007	17769.10	482.67	-15,223.24	-122.05	231746975.20	14895.23	1857935.30
2008	27529.30	532.65	-5,463.04	-72.07	29844784.19	5193.51	393699.30
2009	36827.16	585.95	3,834.82	-18.77	14705859.77	352.16	-71964.27
2010	40948.44	630.13	7,956.10	25.41	63299559.03	645.87	202196.38
2011	41887.69	792.18	8,895.35	187.46	79127287.20	35142.75	1667558.27
	$\sum X =$ 164961.69	$\sum Y =$ 3,023.58			$\sum x^2 =$ 418724465.40	$\sum y^2 =$ 56229.52	$\sum xy =$ 4049424.98

We have, Karl Pearson Correlation Coefficient,

Correlation Coefficient (r) = $\dfrac{\sum xy}{N \pm_x \pm_y}$

On implication of the equation of r, we obtain the following formula for computing r.

Correlation Coefficient (r) = $\dfrac{\sum xy}{\sqrt{\sum x^2 \sum y^2}} = \dfrac{(4049424.98)}{\sqrt{418724465.40 \times 56229.52}} = 0.8345$

Probable Error (P.E.) = $\dfrac{0.6745\,(1 - r^2)}{\sqrt{N}} = \dfrac{0.6745\left[1 - (0.8345)^2\right]}{\sqrt{5}} = 0.0916$

6 P.E. = 6 × 0.0916 = 0.5496

Similarly the Correlation Coefficients, P.E. and 6 P.E. between different variables of NIBL have been calculated.

Appendix - E

Calculation of Correlation Coefficient, P.E. and 6*P.E. of HBL (Sample Calculation)

(Rs. in Million)

Year (Mid July)	Loan and Advances (X)	LLP (Y)	$x = X - \overline{X}$	$y = Y - \overline{Y}$	x^2	y^2	$x \times y$
2007	17793.72	795.73	-7323.25	-153.99	53630049.15	23712.92	1127707.88
2008	20179.61	682.09	-4937.36	-267.63	24377563.27	71625.82	1321386.73
2009	25519.52	726.36	402.55	-223.36	162043.28	49889.69	-89912.67
2010	29123.75	1143.13	4006.78	193.41	16054253.91	37407.43	774950.55
2011	32968.27	1401.29	7851.30	451.57	61642848.88	203915.46	3545409.73
	$\sum X =$ 125584.87	$\sum Y =$ 4748.60			$\sum x^2 =$ 155866758.49	$\sum y^2 =$ 386551.32	$\sum xy =$ 6679542.22

We have, Karl Pearson Correlation Coefficient,

Correlation Coefficient (r) = $\dfrac{\sum xy}{N \pm_x \pm_y}$

On implication of the equation of r, we obtain the following formula for computing r.

Correlation Coefficient (r) = $\dfrac{\sum xy}{\sqrt{\sum x^2 \sum y^2}} = \dfrac{6679542.22}{\sqrt{155866758.49 \times 386551.32}} = 0.8605$

Probable Error (P.E.**) =** $\dfrac{0.6745\,(1 - r^2)}{\sqrt{N}} = \dfrac{0.6745\left[1 - (0.8605)^2\right]}{\sqrt{5}} = 0.0783$

6 P.E. = 6 × 0.0783 = 0.4698

Similarly the Correlation Coefficients, P.E. and 6 P.E. between different variables of HBL have been calculated.

Appendix - F

Calculation of Trend values of Loans and Advances of NIBL (Sample Calculation)

(Rs. in Million)

Year (Mid July) (t)	Loan & Advances (Y)	Deviation from Mid July X= t-2009	$X \times Y$	X^2	$Yc = a + bX$
2007	17769.10	-2	-35538.20	4	20661.07
2008	27529.30	-1	-27529.30	1	26826.71
2009	36827.16	0	0.00	0	32992.34
2010	40948.44	1	40948.44	1	39157.97
2011	41887.69	2	83775.38	4	45323.60
	$\sum Y$ = 164961.69	$\sum X = 0$	$\sum XY$ = 61656.32	$\sum X^2 = 10$	

Here,

When ∑X= 0, from the two normal equations,

$$a = \frac{\sum Y}{N} = \frac{164961.69}{5} = 32992.34$$

$$b = \frac{\sum XY}{X^2} = \frac{61656.32}{10} = 6165.63$$

Thus,

Average Loans & Advances (a) = Rs. 32,992.34

Rate of change of loans and advances (b) = Rs. 6,165.63

Hence the equation of straight line trend is

$Yc = a+bX$

$Yc = 32992.34+6165.63$ ò X

Expected trend values of Loans and Advances (2012-2016)

Years (Mid July)	Deviation from Mid July 2009	$Yc = a + bX$ $Yc = 32992.34 + 6165.63 \times X$
2012	3	51489.23
2013	4	57654.87
2014	5	63820.50
2015	6	69986.13
2016	7	76151.76

Similarly the Trend Values different variables of NIBL have been calculated.

Appendix - G

Calculation of Trend values of Loans and Advances of HBL (Sample Calculation)

(Rs. in Million)

Year (Mid July) (t)	Loan & Advances (Y)	Deviation from Mid July X= t-2009	$X \times Y$	X^2	$Yc = a + bX$
2007	17793.72	-2	-35587.44	4	17258.33
2008	20179.61	-1	-20179.61	1	21187.65
2009	25519.52	0	0.00	0	25116.97
2010	29123.75	1	29123.75	1	29046.30
2011	32968.27	2	65936.54	4	32975.62
	$\sum Y$ = 125584.87	$\sum X = 0$	$\sum XY$ = 39293.24	$\sum X^2 = 10$	

Here,

When ∑X= 0, from the two normal equations,

$$a = \frac{\sum Y}{N} = \frac{125584.87}{5} = 25116.97$$

$$b = \frac{\sum XY}{X^2} = \frac{39293.24}{10} = 3929.32$$

Thus,

Average Loans & Advances (a) = Rs. 25,116.97

Rate of change of loans and advances (b) = Rs. 3,929.32

Hence the equation of straight line trend is

$Yc = a+bX$

$Yc = 25116.97+3929.32 \times X$

Expected trend values of Loans and Advances (2012-2016)

Years (Mid July)	Deviation from Mid July 2009	$Yc = a + bX$ $Yc = 25116.97 + 3929.32 \times X$
2012	3	36904.95
2013	4	40834.27
2014	5	44763.59
2015	6	48692.92
2016	7	52622.24

Similarly the Trend Values different variables of HBL have been calculated.

Appendix - H

INTERVIEW QUESTIONNAIRE FOR BANK OFFICIALS

Name : …………………………………………

Institution : …………………………………………

Address : ……………………………………….…

1. How important do you think is the directives related to loan classification and provisioning for a commercial bank?

   ☐ Very important
   ☐ Not important

2. Do you think, the present directives related to loan classification and provisioning is appropriate and better than the previous one?

   ☐ Yes
   ☐ No

3. What will be the impact of new directives on provision for loan loss of commercial banks?

   ☐ Will increase provision for loan loss.
   ☐ Will decrease provision for loan loss.
   ☐ Will have no impact.
   ☐ Others

4. How do you think the shareholders of the bank are going to be affected by the present loan classification and provisioning directives?

   ☐ Will enjoy lesser dividend.
   ☐ Will have their EPS decreased.
   ☐ Will not be affected at all.
   ☐ Others

5. How do you think, will the banks cope with the problem brought about by this amendment of loan classification and provisioning directives? Specifically what are the alternatives your management is pondering to cope with the problem thus created?

- ☐ Will control the credit disbursal by being more stringent.
- ☐ Will strengthen the monitoring and follow up procedures.
- ☐ Will negotiate with Nepal Rastra Bank on the directives.
- ☐ Others

6. To what extent, today's banking industry is effected by the problem of NPA?

- ☐ Not affected.
- ☐ Nominally affected
- ☐ Moderately affected
- ☐ Severely affected.

7. Which measure is the best option to resolve the problem of NPA?

- ☐ Setting up recovery cell
- ☐ Hiring Asset Management Company (AMC)
- ☐ Others

8. What are the major factors, which lead to increasing NPA? (Please Rate)

- ☐ Improper credit appraisal system.
- ☐ Economic slowdown/recession.
- ☐ Ineffective credit monitoring and supervision system.
- ☐ Political pressure to lend to un-creditworthy borrowers
- ☐ Others

Appendix – H-1

Analysis of Interviews Questionnaire for Bank Officials:

Question No. 1	No. of Responses	Percentage
(a) Very important	12	100 %
(b) Not important	0	0 %

Question No. 2	No. of Responses	Percentage
(a) Yes	9	75 %
(b) No	3	25 %

Question No. 3	No. of Responses	Percentage
(a) Will increase provision for loan loss	12	100 %
(b) Will decrease provision for loan loss	0	0 %
(c) Will have no impact	0	0 %
(d) Others	0	0 %

Question No. 4	No. of Responses	Percentage
(a) Will enjoy lesser dividend	5	41.67 %
(b) Will have their EPS decreased	7	58.33 %
(c) Will not be affected at all	0	0 %
(d) Others	0	0 %

Question No. 5		No. of Responses	Percentage
(a)	Will Control the credit disbursal by being more stringent	8	66.67 %
(b)	Will strengthen the monitoring and follow up procedures	4	33.33 %
(c)	Will negotiate with Nepal Rastra Bank on the directives	0	0 %
(d)	Others	0	0 %

Question No. 6		No. of Responses	Percentage
(e)	Not affected	0	0 %
(f)	Nominally affected	0	0 %
(g)	Moderately affected	3	25 %
(h)	Severely affected	9	75 %

Question No. 7		No. of Responses	Percentage
(a)	Setting up recovery cell	10	83.33 %
(b)	Hiring Asset Management Company (AMC)	2	16.67 %
(c)	Others	0	0 %

Question No. 8		No. of Responses	Percentage
(a)	Improper credit appraisal system	2	16.67 %
(b)	Economic slowdown/ recession	5	41.67 %
(c)	Ineffective credit monitoring and supervision system	3	25 %
(d)	Political pressure to lend to un-creditworthy borrowers	2	16.67 %
(e)	Others	0	0 %