

CHAPTER – I

INTRODUCTION

1.1 Background of the Study

Banks are the financial backbone for economic development of any country. Without a sound banking system a country cannot have a healthy economy. A bank is a financial institution which deals with money and credit. It accepts deposits from individuals, firms and companies at a lower rate of interest and gives it at a higher rate of interest to those who need them. The difference between the terms at which it borrows and which it lends forms the source of profit, thus bank being a profit earning institute.

For the development of any country, the financial sector of that country is responsible and must be strong. The financial sector is important and is a vast field, which includes banks, finance company, co-operative, insurance companies, stock exchange, foreign exchange market, mutual fund, employee provident fund etc. These institutions collect idle and scattered money from the general public and organization and finally invest in different needy enterprises that consequently help in increasing employment opportunities, reducing poverty and thereby developing the society and the nation as a whole.

Lending is the provision of monetary resources by the banker where the other party reimburses in installments or any other form of deferred payment, thereby by generating a debt. Loans and advances portfolio being the most significant asset of the bank has direct impact on its profitability. Increase in competition and emergence of new types of risks in the banking sector has lead to efficient loans and advances management. In order to ensure a strong portfolio banks need to implement necessary policies aiming at strengthening of pre sanction appraisal and post sanction monitoring system. In order to cope up with the

changing scenario, banks in Nepal are strengthening their organizational setup through specialized departments to meet the credit requirements of the borrowers and continuous analysis of the potential credit growth.

Going through loan granting provision, bank will look through safety of funds, purpose of loans, security for loans, profitability spread of loan portfolio etc. Besides this, the character of person receiving credit, the capacity of borrower to utilize the fund, the percentage of borrower stake in the business are the basic elements which measures the quality of borrower and ultimately the quantity of the loan.

Nepal has been facing the problem of accelerating the pace of economic development. Economic development of the any country depends upon the uplift meant of the people through increasing their productivity thereby raising their incomes, which ultimately help them to cross the poverty line. In this respect the role of commercial banks in the country becomes vital. The commercial banking system in Nepal is still in its infant stage as compared to other developed countries. However their important role in the economic development of the country has been fully realized and these banks are being oriented in their activities to make best suited for the overall economic development of the country.

This way bank plays an important part in the development of trade, commerce and industry. Today no banker can survive for long run without proper standing of economy and economy cannot pace ahead without proper banking system built.

1.1.1 Profile of Rastriya Banijya Bank Limited

Rastriya Banijya Bank (RBB) is fully government owned, and the largest commercial bank in Nepal. RBB was established on January 23, 1966 (2022 Magh 10 BS) under the RBB Act. RBB provides various banking services to a

wide range of customers including banks, insurance companies, industrial trading houses, airlines, hotels, and many other sectors.

RBB has Nepal's most extensive banking network with over 124 branches. Through its branch network, RBB has been contributing to Nepal's economic development by providing banking services throughout the country.

RBB has many correspondent arrangements with major international banks all over the world that facilitate trade finance, bank-originated personal funds transfers and interbank funds transfer via SWIFT. In a bid to promote remittance business, RBB works with Western Union and International Money Express, two leading person-to-person funds transfer networks.

In addition RBB runs various programmes i.e. Banking with the Poor, Micro Credit project for Women etc. to enhance the living standard of people as per the govt. directives.

As well, RBB actively delivers various government programs to people living in remote parts of the country; these programs are intended to raise living standards.

1.2 Statement of the Problem

Due to globalization and liberalization of economy, the number of commercial banks is increasing in Nepal. But the banking service per person is very low. Poorer or deprived sector of the economy is granted loan only due to the strict directives set by Nepal Rastra Bank (NRB). Banks are not easily accessible to the people of remote and village areas because commercial banks are established mostly in the cities and capital of the country.

The main function of commercial bank is loan management. It is very challenging task on the part of bank because the bank has to disburse loan in

the appropriate sector and recover it in time as well. In this competitive environment, it is very difficult to choose right and productive sectors for granting loan. Hence, there is the chance of flowing bank's deposit in unproductive sector.

Rastriya Banijya Bank (RBB) is one of the oldest banks of Nepal. RBB is committed for economic and industrial development of the country. But this bank does not have successful results and operations. Due to tough competition and lack of peace and political instability, these banks are facing problems on loan investment and recovery patterns due to lack of supervision the loan granted by these banks for one purpose is used for another. Similarly, the lending procedures are cumbersome and lengthy. The terms, conditions and languages are unfamiliar to the general people. The problem of the study is directed to find the solution of following questions.

- a. Whether the loan investment and loan recovery satisfactory in relation to loan outstanding?
- b. To what extent, the growth rate of loan outstanding, loan recovery and loan investment of the bank is raising on?
- c. Is the bank efficient in controlling non performing loan, and keeping the sufficient provision on loan loss?
- d. What is the relationship of loan and advances with net profit and total deposit?
- e. What will be the loan and advances of the bank in the forthcoming years?

1.3 Objectives of the Study

The main objective of this study is to analyze, examine and interpret the loan management of RBB. The other specific objectives of the study are as follows;

- a. To evaluate loan investment and loan recovery in relation to loan outstanding.

- b. To measure the growth rate of loan outstanding, loan recovery and loan investment.
- c. To analyze the non performing loan of the banks and the provision made for default loan.
- d. To measure the deposit mobilization rate on loan and advances and the relationship of loan and advances with net profit.
- e. To estimate the value of loan and advances for the next four year periods.

1.4 Significance of the Study

The study will be mainly beneficial to the shareholders, depositors and other creditors to identify the productivity of their funds in the RBB. Likewise other financial agencies, e.g. financial experts are also interested in the performance of bank. Besides them, the study will also help the management of the bank to analyze the effectiveness of its loan management and policies of the bank in comparison to competitors. The study will also be equally significant to the central bank to formulate the new credit policy, as there are certain loopholes as a result of which the non-performing assets has been regarded as the main problem of the commercial banks in these days.

1.5 Limitations of the Study

The research study has some limitations. The main limitations of the study are as follows: -

- a. Though, there has been in operation of 26 commercial banks in Nepal, only RBB is taken for the proposed study and thus may not represent the whole population.
- b. This study concentrates only on loan management and thus ignores the other financial aspects.
- c. The secondary data will be used for presentation and interpretation. Only a 10-years data will be considered. The reliability of the data depends totally on the annual reports of the bank.

- d. In this study, only selected financial and statistical tools as well as techniques are used.

1.6 Organization of the Study

The whole study is divided into five different chapters. They are:

Chapter – I: Introduction

This chapter includes background of the study, the profile of RBB, statement of the problems, objectives of the study, significance of the study, and limitations of the study and organization of the study.

Chapter – II: Review of Literature

This chapter deals with review of literatures, which includes conceptual/theoretical review and review of related studies. Further, the chapter traces out the research gap of the previous studies.

Chapter – III: Research Methodology

This chapter is related to research methodology employed. It includes research design, population and sample, source of data, data collection techniques and data analysis tools.

Chapter – IV: Data Presentation and Analysis

The fourth chapter deals with the data analysis and interpretations of data relating to loan & advances. It also presents major finding of the study.

Chapter – V: Summary, Conclusion and Recommendations

It includes summary and conclusion of the study. Further, recommendations are presented on the basis of findings and conclusions drawn.

Besides these, **Bibliography** and **Appendix** are presented at the end of the study.

CHAPTER – II

REVIEW OF LITERATURE

This part of the study deals with making theoretical framework. So, it incorporates the review of concepts, review of journals and articles and review of thesis.

2.1 Conceptual Framework

“Effective management of the loan and the credit function is fundamental to a bank’s safety and soundness. Loan management (LM) is the process by which risks that are inherent in the credit process are managed and controlled. Because review of the LM process is so important, it is a primary supervisory activity. Assessing LM involves evaluating the steps bank management takes to identify and control risk throughout the credit process. The assessment focuses on what management does to identify issues before they become problems” (Rose; 2002: 47).

“Lending is the principal business activity for most commercial banks. The loan is typically the largest asset and the predominate source of revenue. As such, it is one of the greatest sources of risk to a bank’s safety and soundness. Whether due to lax credit standards, poor risk management, or weakness in the economy, loan problems have historically been the major cause of bank losses and failures” (Khan; 1982: 110).

For decades, good loan portfolio managers have concentrated most of their effort on prudently approving loans and carefully monitoring loan performance. Although these activities continue to be mainstays of loan portfolio management, analysis of past credit problems, such as those associated with oil and gas lending, agricultural lending, and commercial real estate lending in the 1980s, has made it clear that portfolio managers should do more. Traditional practices rely too much on trailing indicators of credit

quality such as delinquency, nonaccrual, and risk rating trends. Banks have found that these indicators do not provide sufficient lead time for corrective action when there is a systemic increase in risk.

2.1.1 Risks Associated with Lending

“Lending can expose a bank’s earnings and capital to all of the risks. Therefore, it is important that the examiner assigned LM understands all the risks embedded in the loan and their potential impact on the institution. Risk is the potential that events, expected or unexpected, may have an adverse impact on the bank’s earnings or capital. A key challenge in managing risk is to understand the interrelationships of the nine risk factors” (Gitman & Jochnk; 1990: 23).

a) Credit Risk

Credit risk arises due to possibility of payment default from the counter parties. For most banks, loans are the largest and most obvious source of credit risk. However, there are other pockets of credit risk both on and off balance sheet, such as the investment portfolio, overdrafts, and letters of credit. Many products, activities, and services, such as derivatives, foreign exchange, and cash management services, also expose a bank to credit risk.

“The risk of repayment, i.e., the possibility that an obligor will fail to perform as agreed, is either lessened or increased by a bank’s credit risk management practices. A bank’s first defense against excessive credit risk is the initial credit-granting process, sound underwriting standards, an efficient, balanced approval process, and a competent lending staff. Because a bank cannot easily overcome borrowers with questionable capacity or character, these factors exert a strong influence on credit quality. Borrowers whose financial performance is poor or marginal, or whose repayment ability is dependent upon unproven projections can quickly become impaired by personal or external economic stress. Management of credit risk, however, must continue

after a loan has been made, for sound initial credit decisions can be undermined by improper loan structuring or inadequate monitoring” (Gitman & Jochnk; 1990: 27).

b) Interest Rate Risk

The level of interest rate risk attributed to the bank’s lending activities depends on the composition of its loan portfolio and the degree to which the terms of its loans (e.g., maturity, rate structure, embedded options) expose the bank’s revenue stream to changes in rates.

“Pricing and portfolio maturity decisions should be made with an eye to funding costs and maturities. When significant individual credits or portfolio segments are especially sensitive to interest rate risk, they should be periodically stress-tested. If the asset/liability management committee (ALCO), which typically is responsible for managing the bank’s interest rate risk, is to manage all of the bank’s positions, it must have sufficient reports on loan portfolio and pipeline composition and trends. These reports might include a maturing loans report, pipeline report, and rate and repricing report.” (Francis; 1991: 52).

Banks frequently shift interest rate risk to their borrowers by structuring loans with variable interest rates. Borrowers with marginal repayment capacity may experience financial difficulty if the interest rates on these loans increase. As part of the risk management process, banks should identify borrowers whose loans have heightened sensitivity to interest rate changes and develop strategies to mitigate the risk. One method is to require vulnerable borrowers to purchase interest rate protection or otherwise hedge the risk.

c) Liquidity Risk

“Because of the size of the loan, effective management of liquidity risk requires that there be close ties to, and good information flow from, the lending

function. Obviously, loans are a primary use of funds. And while controlling loan growth has always been a large part of liquidity management, historically the loan has not been viewed as a significant source of funds for liquidity management. Practices are changing, however. Banks can use the loan portfolio as a source of funds by reducing the total dollar volume of loans through sales, securitization, and portfolio run-off” (Francis; 1991: 55).

In fact, banks are taking a more active role in managing their loan portfolios. While these activities are often initiated to manage credit risk, they have also improved liquidity. Banks increasingly are originating loans “for sale” or securitization. Consumer loans (mortgages, installment loans, and credit cards) are routinely originated for immediate securitization. Many larger banks have been expanding their underwriting for the syndicated loan market.

d) Price Risk

Most of the developments that improve the loan portfolio’s liquidity have implications for price risk. Traditionally, the lending activities of most banks were not affected by price risk. Because loans were customarily held to maturity, accounting doctrine required book value accounting treatment. However, as banks develop more active portfolio management practices and the market for loans expands and deepens, loan portfolios will become increasingly sensitive to price risk.

“Loans originated for sale as part of a securitization or for direct placement in the secondary market carry price risk while they are in the pipeline awaiting packaging and sale. During that period, the assets should be placed in a “held-for-sale” account, where they must be repriced at the lower of cost or market. The same accounting treatment can apply to syndicated credits and distressed loans. When a bank underwrites a larger portion of a syndicated loan than its “hold” position, the excess portion must be placed in a held-for- sale account. Once a sale strategy is adopted for distressed or otherwise undesirable credits,

those credits should also be placed in a held-for-sale account” (Gitman & Jochnk; 1990: 31).

e) Foreign Exchange Risk

“Foreign exchange risk is present when a loan or portfolio of loans is denominated in a foreign currency or is funded by borrowings in another currency. In some cases, banks will enter into multi-currency credit commitments that permit borrowers to select the currency they prefer to use in each rollover period. Foreign exchange risk can be intensified by political, social, or economic developments. The consequences can be unfavorable if one of the currencies involved becomes subject to stringent exchange controls or is subject to wide exchange-rate fluctuations” (Gupta; 1984: 213).

f) Transaction Risk

In the lending area, transaction risk is present primarily in the loan disbursement and credit administration processes. “The level of transaction risk depends on the adequacy of information systems and controls, the quality of operating procedures, and the capability and integrity of employees. Significant losses in loan and lease portfolios have resulted from inadequate information systems, procedures, and controls” (Gupta; 1984: 215). For example, banks have incurred increased credit risk when information systems failed to provide adequate information to identify concentrations, expired facilities, or stale financial statements. At times, banks have incurred losses because they failed to perfect or renew collateral liens; to obtain proper signatures on loan documents; or to disburse loan proceeds as required by the loan documents.

g) Compliance Risk

“Lending activities encompass a broad range of compliance responsibilities and risks. By law, a bank must observe limits on its loans to a single borrower, to insiders, and to affiliates; limits on interest rates; and the array of consumer

protection and Community Reinvestment Act regulations. A bank's lending activities may expose it to liability for the cleanup of environmental hazards. A bank may also become the subject of borrower-initiated "lender liability" lawsuits for damages attributed to its lending or collection practices. Supervisory activities should include the review of the bank's internal compliance process to ensure that examiners identify and investigate compliance issues" (Desai; 1967: 37).

h) Strategic Risk

"A primary objective of loan portfolio management is to control the strategic risk associated with a bank's lending activities. Inappropriate strategic or tactical decisions about underwriting standards, loan portfolio growth, new loan products, or geographic and demographic markets can compromise a bank's future. Examiners should be particularly attentive to new business and product ventures. These ventures require significant planning and careful oversight to ensure the risks are appropriately identified and managed. Both bankers and examiners need to decide whether the opportunities outweigh the strategic risks. If a bank is considering growing a loan product or business in a market saturated with that product or business, it should make sure that it is not overlooking other lending opportunities with more promise. During their evaluation of the loan management process, examiners should ensure that bankers are realistically assessing strategic risk" (Desai; 1967: 40).

i) Reputation Risk

When a bank experiences credit problems, its reputation with investors, the community, and even individual customers usually suffers. Inefficient loan delivery systems, failure to adequately meet the credit needs of the community, and lender-liability lawsuits are also examples of how a bank's reputation can be tarnished because of problems within its lending division.

"Reputation risk can damage a bank's business in many ways. The value of the bank's stock falls, customers and community support is lost, and business

opportunities evaporate. To protect their reputations, banks often feel that they must do more than is legally required. For example, some banks have repurchased loan participations when credit problems develop, even though these problems were not apparent at the time of the underwriting” (Francis; 1991: 60).

2.1.2 Loan Management Objectives

“Loan objectives establish specific, measurable goals for the bank. The board of directors must ensure that loans are made with the following three basic objectives in mind:” (Crosse; 1963: 73)

- To grant loans on a sound and collectible basis.
- To invest the bank’s funds profitably for the benefit of shareholders and the protection of depositors.
- To serve the legitimate credit needs of their communities.

2.1.2.1 Strategic Planning for the Loan

“For most banks, meeting the aforementioned three objectives will require that senior management and the board of directors develop medium- and long-term strategic plans and objectives for the loan portfolio. These strategies should be consistent with the strategic direction and risk tolerance of the institution. They should be developed with a clear understanding of their risk/reward consequences. They also should be reviewed periodically and modified as appropriate. In drawing up strategic objectives, management and the board should consider establishing:” (Crosse; 1963: 85)

- What proportion of the balance sheet, the loan should comprise?
 - Goals for loan quality.
 - Goals for portfolio diversification.
- How much the loan should contribute to the bank’s financial objectives?
 - Loan product mix.

- Loan growth targets by product, market, and portfolio segment.
- Product specialization.
- What the bank's geographic markets should be?
 - Targeted industries.
 - Targeted market share.
 - Community needs and service.
 - General financial objectives (e.g., increase fee income).

The bank's loan policies, underwriting guidelines, and procedures should communicate and support the strategic objectives for the portfolio. MIS should be able to inform management about whether performance measures up to plans. Management should evaluate business, marketing, and compensation plans to ensure that short-term goals and incentives are consistent with strategic portfolio objectives and risk tolerances. In community banks without formal strategic plans, senior management should be able to articulate the bank's strategic objectives. It should be evident, as well, that the board of directors has endorsed those objectives.

2.1.3 The Loan Policy

The loan policy is the primary means by which senior management and the board guide lending activities. Although the policy primarily imposes standards, it also is a statement of the bank's basic credit philosophy. It provides a framework for achieving asset quality and earnings objectives, sets risk tolerance levels, and guides the bank's lending activities in a manner consistent with the bank's strategic direction. Loan policy sets standards for portfolio composition, individual credit decisions, fair lending, and compliance management.

“Loan policies vary in length, organization, degree of detail, and breadth of topics, there is no ideal format. Frequently, the bank's general lending policy

will be supplemented by more detailed underwriting standards, guidelines, and procedures. Within the same banking company, certain aspects of the policy may vary because of factors such as geographic location, economic conditions, personnel, or portfolio objectives. The format should be tailored to fit the needs of a particular bank, and the scope and detail should be commensurate with the complexity of the bank's lending activities" (William; 1960: 104).

In all but very small community banks, the loan policy will be written. "The policy should provide a realistic description of where the bank wants to position itself on the risk/reward spectrum. It needs to provide sufficient latitude for a bank to respond to good business opportunities while concurrently controlling credit risk. In normal circumstances, a bank should be able to achieve portfolio objectives and respond to changing market conditions without triggering a limit. Limits should not be so conservative that insignificant changes breach them, nor should they be so liberal that they have no practical effect" (Grywinski: 1991: 75).

"For the policy to be an effective risk management tool, it must clearly establish the responsibilities of those involved in the lending process. For example, who is authorized to approve a covenant violation, who arbitrates risk rating differences, can a credit-scored decision be overridden? Lenders must know what is expected of them. When policy is vague or too broad, credit standards may be unclear and virtually nothing may be regarded as an exception. If the policy states that a bank will extend credit to established businesses, almost any company would qualify. But a policy further requiring the business to be profitable, in operation for at least two years, and located within the bank's community is providing meaningful guidance" (Grywinski: 1991: 77).

When policy is too prescriptive and particular, exceptions to policy will become the rule and meaningless exception data will mask meaningful trends,

thereby diminishing the effectiveness of the policy. Because exceptions are so important, the policy should address them specifically; it should state when they are acceptable and how they should be identified, mitigated, and documented. Some lending standards, such as those that implement legal requirements or those whose violation quickly translates into losses, have greater significance than others. More substantive exceptions should have heightened reporting requirements to senior management and the board. Failure to comply with the provisions of loan policy concerning exceptions is generally regarded as a material weakness.

“Policies should be periodically reviewed and revised to accommodate changes in the bank’s strategic direction, risk tolerance, or market conditions. Policy review should consider the organizational structure, breadth and complexity of lending activities, capabilities and skills of lending personnel, and strategic portfolio quality and earnings objectives. Changes in regulations and business conditions also need to be considered. In addition to providing an opportunity for change, the review should evaluate how well the policy has guided lending decisions. For example, a high volume of exceptions indicates that many loan decisions are being made outside the policy. This could mean that the bank is assuming more risk than is desirable or that the policy is too restrictive. If the bank’s policy is too restrictive, easing it could increase business opportunities without unduly increasing risk. Conversely, the absence of exceptions may indicate that the policy is too vague, and a tightening of the policy could strengthen the controls on loan quality. All policy reviews should include the organizational unit responsible for assessing compliance with policy” (Reed, Edward, Cotter & Smith; 1980: 82).

2.1.3.1 Loan Policy Topics

“While the form and contents of loan policies and procedures will vary from bank to bank, there are some topics that should be covered in all cases. These are:” (Chopra; 1989: 17)

- Loan authorities.
- Limits on aggregate loans and commitments.
- Portfolio distribution by loan category and product.
- Geographic limits.
- Desirable types of loans.
- Underwriting criteria.
- Financial information and analysis requirements.
- Collateral and structure requirements.
- Margin requirements.
- Pricing guidelines.
- Documentation standards.
- Collections and charge-offs.
- Reporting requirements.
- Guidelines for loan participations.
- Off-balance-sheet exposure.

The policy may also address insider transactions, affiliate transactions, conflicts of interest, the code of ethics, community support, appraisal requirements, environmental assessment requirements, relevant accounting issues (such as charge-off loans, nonperforming loans, and debt restructuring), and the allowance for loan and lease losses. Any administrative requirements for granting loans should be covered in the policy. Policies and procedures should also ensure compliance with laws and regulations.

2.1.4 Loan Approval Process

The loan approval process is the first step towards good portfolio quality. When individual credits are underwritten with sound credit principles, the credit quality of the portfolio is much more likely to be sound. Although good loans sometimes go bad, a loan that starts out bad is likely to stay that way. The foremost means to control loan quality is a solid loan approval process.

“Every loan approval process should introduce sufficient controls to ensure acceptable credit quality at origination. The process should be compatible with the bank’s credit culture, its risk profile, and the capabilities of its lenders. Further, the system for loan approvals needs to establish accountability.

Each method of loan approval has inherent strengths and weaknesses. The committee method is advantageous because knowledge can be shared, but it may diminish accountability and often slows a bank’s responsiveness. The individual signature authority system is more timely and establishes clear accountability, but it can create undue credit risk if a lender’s knowledge and experience are inadequate to his or her authority” (Diamond; 1960: 173).

Laddered or joint authorities, variations that some banks employ, combine elements of both systems. The involvement of an independent loan approval authority whose primary goal is quality (such authority might be invested in a senior credit officer or credit administrator) is also a method to introduce more objectivity to the loan approval process. Whatever approach or combination of approaches a bank uses, internal control mechanisms are necessary to ensure that the approval system produces sound credit decisions.

“An effective loan approval process establishes minimum requirements for the information and analysis upon which a credit decision is based. It provides guidance on the documents needed to approve new credit, renew credit, increase credit to existing borrowers, and change terms in previously approved credits. It will also designate who has the authority to approve credit or changes in credit terms. Loan authorities should be commensurate with the experience of the lender/credit officer and take into consideration the type of credit, the amount of credit, and the level of risk involved. Generally, underwriting document standards should include:” (Dahal & Dahal; 2007: 39)

- Financial information including:

- a. current and historical balance sheet and income data,
 - b. balance sheet, income, and cash flow projections, when appropriate, and comparative industry data when appropriate.
- Financial analysis, including repayment capacity.
 - Collateral identification and valuation.
 - Guarantor support and related financial information.
 - Summary of borrower and affiliated credit relationships.
 - Loan terms, including tenor and repayment structure.
 - Pricing information, including relationship profitability data.
 - Covenants and requirements for future submission of financial data.
 - Exceptions to policy and underwriting guidelines.
 - Information fields to capture data for concentration reporting, identifying SNCs (shared national credits), etc.
 - Risk rating or recommended risk rating.

The approval process for consumer loans may be more streamlined, but should still include sufficient information to support the credit granting decision, including, when applicable, scorecard data.

2.1.5 Loan Portfolio Management

To manage the loan portfolio effectively, the bank should consider the following factors.

2.1.5.1 Risk Identification

“Effective risk identification starts with the evaluation of individual credits. Rating the risk of each loan in timely credit evaluations is fundamental to loan portfolio management. Some banks apply risk ratings to relationships, others prefer to rate each facility, and still others rate both relationships and facilities. Risk ratings should also be applied to off-balance-sheet exposures like letters of credit and unfunded commitments that the bank is obligated to fund unless there is a default. These evaluations allow the prompt detection of changes in

portfolio quality, enabling management to modify portfolio strategies and intensify the supervision of weaker credits in a timely manner” (Joseph; 1998: 10).

2.1.5.2 Exceptions to Policy, Procedures, and Underwriting Guidelines

“Lending exceptions generally either relate to documentation or underwriting. Banks should have systems to analyze and control both types of exceptions. While it is advisable to identify, mitigate, and monitor all exceptions, the level of attention and reporting should correspond with the materiality of the exception” (Joseph; 1998: 10).

a) Documentation Exceptions

“Loan documentation” refers broadly to the documents needed to legally enforce the loan agreement and properly analyze the borrower’s financial capacity. When a document is missing, stale, or improperly executed, it becomes an exception. Common loan documents are promissory notes, note guarantees, financial statements, collateral agreements, and appraisals. The promissory note, guarantee, and financial statement must be properly prepared and signed; the financial statement must be received and analyzed in a timely manner by the bank; and the collateral agreement must be recorded in the appropriate jurisdiction” (Joseph; 1998: 11).

b) Policy and Underwriting Exceptions

“Policy and underwriting exceptions are conditions in approved loans that violate the loan policy or underwriting guidelines. Because underwriting guidelines are the primary means by which the bank steers lending decisions toward planned strategic objectives and maintains desired levels of risk within the portfolio, deviations from these guidelines should be well documented and justified” (Joseph; 1998: 11).

2.1.5.3 Aggregate Exception Tracking and Reporting

“Tracking the aggregate level of exceptions helps detect shifts in the risk characteristics of loan portfolios. In consumer lending, where such tracking is common, it has facilitated risk evaluation, strengthened portfolio liquidity, and helped management to identify new business opportunities. Similar benefits can accrue from tracking underwriting exceptions in commercial and real estate loan portfolios” (Joseph; 1998: 13).

2.1.5.4 Portfolio Segmentation and Risk Diversification

“Risk diversification is a basic tenet of portfolio management. Concentrations of credit risk occur within a portfolio when otherwise unrelated loans are linked by a common characteristic. If this common characteristic becomes a common source of weakness for the loans in concentration, the loans could pose considerable risk to earnings and capital” (Joseph; 1998: 13).

a) Identifying Concentrations of Risk

“Managing the loan portfolio includes managing any concentrations of risk. By segmenting the portfolio into pools of loans with similar characteristics, management can evaluate them in light of the bank’s portfolio objectives and risk tolerances and, when necessary, develop strategies for reducing, diversifying, or otherwise mitigating the associated risks” (Joseph; 1998: 14).

2.1.5.5 Evaluating and Managing Concentrations of Risk

“Each pool should be evaluated individually — that is, as a discrete pool of risk — and as part of the whole — that is, by how it fits into the portfolio and supports loan portfolio goals. A large exposure to one type of borrower or industry may well be less risky than a small exposure to another. The goal is to achieve the desired balance of risk and return for the portfolio as a whole.” (Joseph; 1998: 15).

a) Concentration Management Techniques

“Over the past decade, banks, especially large ones, have been adopting more active portfolio management practices. They are expanding their MIS capabilities and strengthening their credit risk management practices. There are a variety of techniques banks can use to manage portfolios and control concentration risk.

The most common tool is setting exposure limits, or ceilings, on concentrations. Diversifying away from a limit can be accomplished by reducing certain exposures or increasing the borrower base. The reduction of exposures begins with a reassessment of individual borrowers’ needs and requires considerable discipline. Nonetheless, it can be a useful tool to diversify risk over a larger customer base.

A bank can change the distribution of its assets by increasing the geographic diversification of borrowers; altering the bank’s product mix (for example, by reducing commercial lending and increasing consumer lending); or changing the risk profile of the bank’s target market (for example, by turning from middle-market, non-investment-grade customers to well-capitalized, investment-grade customers). Asset sales can also be used to manage concentrations. Banks sell whole loans, sell a portion of a loan into syndication, sell participations in a loan, and securitize certain types of loans. Each of these approaches entails risk/reward trade-offs that must be evaluated in light of the bank’s strategic objectives” (Joseph; 1998: 15).

Recently, banks have begun using credit derivatives to reduce the risk posed by concentrations. Although their usage is modest in all but the largest banks, credit derivatives are gaining acceptance.

2.1.5.6 Stress Testing

“In stress testing, a bank alters assumptions about one or more financial,

structural, or economic variables to determine the potential effect on the performance of a loan, concentration, or portfolio segment. This can be accomplished with “back of the envelope” analysis or by using sophisticated financial models. The method employed is not the issue, rather the issue is asking that critical “what if” question and incorporating the resulting answers into the risk management process. Stress testing is a risk management concept, and all banks will derive benefits, regardless of the sophistication of their methods, from applying this risk management concept to their loans and portfolios” (Joseph; 1998: 16).

1.1.1 2.1.6 NRB Directives

The world has witnessed many financial crises and devastating consequences due to huge financial and economic losses that resulted from each episode. Every crisis was sudden in onset and their, magnitude of losses was much larger than expected. If we go back to the history, then on 3rd march 1997; the Asian crisis began in the form of liquidity problem of two finance companies. Later this spread over to other financial intuition within the Thai financial system. Simultaneously, crisis began to cover Malaysian, Indonesian and South Korean financial statement and loomed in the form of Asian crisis. So this Asian crisis appealed the whole world for regular and timely supervision and assessment of financial system, its soundness and vulnerabilities. This event forced the regulatory authorities for the enforcement of prudential measures in order to avoid further crisis review and revision in prudential regulations such as capital adequacy ratio, asset classification. Provisioning for impaired assets, exposures limit and enforcement of international accounting standard etc have now become common issue all over the world since the late 1990s.

Similarly, in our country too, commercial banks could not recognize the importance of the quality credit and banking sector failed to witness the

expected developments. Subsequently, the banking sector faced the problem of bad debts, overdue loans, accrued interest, accumulation of non-banking assets and excess liquidity in the banking system. In addition to these expected happenings new challenges were added to the Nepalese banking sector due to the adverse development in the domestic economy resulting from deteriorating peace and security situation and continuous persistence of natural calamities inside the country on one hand and the global recession primarily caused by international terrorism on the other. Viewing the need of structural reform amidst these adverse implications, NRB issued directives to run commercial banks in a healthy competitive manner to ensure the sustainable development of the overall banking system.

The financial sector reform of Nepal was initiated in mid 1980s. Since then NRB has been playing a pioneer role in regulation, supervision and monitoring of commercial banks by issuing directives. At present the number of guidelines issued by NRB to commercial banks reaches sixteen, which are as follows.

- 1) The provision of minimum capital fund to be maintained by the commercial bank.
- 2) The provision of loan classifications and loan loss provisioning on the credit.
- 3) The provision relating to limit on credit exposure and facilities to a single borrower, group of related borrowers and single sector of the economy.
- 4) The provision relating to accounting policy and the structure of financial statements to be followed by the commercial banks.
- 5) Regulation relating to minimization of risk inherent in the activities of commercial banks.
- 6) The provision of institutional good governance to be followed by commercial banks.

- 7) Time frame for implementation of regulatory directives issued in connection with inspection and supervision and supervision of commercial banks.
- 8) Regulation relating to investment in shares and securities by commercial banks.
- 9) The provision of submission of statistical data to the NRB. Banking management division and inspection and supervision division.
- 10) Regulation relating to sale and ownership transfer of promoters shares.
- 11) Regulation relating to, stringent blacklisting procedure for loan defaulters.
- 12) The provision relating to compulsory deposited amount of NRB.
- 13) Regulation relating to developing the branch office of commercial banks.
- 14) Provision relating to interest rates.
- 15) Provision relating to collection of financial sources.
- 16) Provision relating to consortium financing.

1.1.2 2.1.6.1 NRB Directives Relating to Loan Classification and Loan Loss Provision (www.nrb.org.np)

1. Classifications of Loan and Advances: Effective from FY 2058/59 (2001/02) banks shall classify outstanding principal amount of loan and advances on the basis of aging. As per the directives issued by NRB, all loans and advances shall be classified into the following four categories:

- a. Pass Loan:** - Loans and advances whose principal amount are not past due and past due for a period up to 3 months shall be included in this category. These are classified and defined as performing loans.
- b. Sub-Standard Loan:** - All loans and advances that are past due for a period of 3 months to 6 months shall be included in this category.

- c. Doubtful Loan:** - All loans and advances which are past due for a period of 6 months to 1 year shall be included in this category.
- d. Loss:** - All loans and advances which are past due for a period of more than 1 year as well as advances which have least possibility of recovery or considered unrecoverable and those having thin possibility of even partial recovery in future shall be included in this category.

Loans and advances falling in this category of sub-standard, Doubtful and loss are classified and defined as Non-performing loan. It is appropriate in the view of the banks management; there is not restriction in classifying the loan and advances from low risk category to high risk category. For instance, loans falling under substandard may be classified into doubtful or loss and loans falling under doubtful may be classified into loss category. The term loan and advances also includes bulls purchased and discounted.

Historical Provisions Relating to Loan Classification is depicted in the following table:

For fiscal year 2001/2002 A.D. (2058/2059 B.S.)

Pass loan	Loans and advances not past due and past due up to 3 months.
Sub-standard loan	Loans and advances past due for a period of over 3 months to 1 year.
Doubtful loan	Loans and advances past due for a period over 1 year to 3 year.
Loss	Loans and advances past due for a period of over 3 Year.

For fiscal year 2002/2003 A.D. (2059/2060 B.S.)

Pass loan	Loans and advances not past due and past due up to 3 months.
Sub-standard loan	Loans and advances past due for a period of over 3 months to 1 year.
Doubtful loan	Loans and advances past due for a period over 1 year to 3 year.
Loss	Loans and advances past due for a period of over 3 Year.

For fiscal year 2003/ 2004A.D. (2060/2061 B.S.)

Pass loan	Loans and advances not past due and past due up to 3 months.
Sub-standard loan	Loans and advances past due for a period of over 3 months to 9 months.
Doubtful loan	Loans and advances past due for a period over 9 months to 2 years.
Loss	Loans and advances past due for a period of over 2 Years.

For fiscal year 2004/2005A.D. (2061/2062 B.S.)

Pass loan	Loans and advances not past due and past due up to 3 months.
Sub-standard loan	Loans and advances past due for a period of over 3 months to 6 months.
Doubtful loan	Loans and advances past due for a period over 6 months to

	1 year.
Loss	Loans and advances past due for a period of over 1 Year.

2. Additional Arrangement in Respect of Pass Loan: Loan and advances fully secured by gold, silver, fixed deposit receipts, credit cards and government securities shall be include under “pass” category. Loans against fixed deposit receipts of other banks shall also qualify for inclusion under pass loan. However, where collateral of fixed deposit receipt or government securities or NRB bonds is placed as extra security, such loan has to be classified on the basis of clause 1 to clause 7. While renewing working capital loan having maturity period up to one year can be classified as pass loan. If the interest of working capital nature loans and advance is not regular, such loan and advances should be classified on the basis of interest outstanding period.

3. Additional Arrangement in Respect of loss Loan: Even if the loan is not past due, loans having any or all of the following discrepancies shall be classified as “loss”.

- a. Security is not sufficient,
- b. The borrower has been declared bankrupt,
- c. The borrower is absconding or cannot be found,
- d. Purchased or discounted bills are not realized within 90 days from the due date and non fund based letter of credit and guarantees etc are not realized with in 90 days from the date of conversion into fund based are not realized within 90 days,
- e. The credit has not been used for the purpose originally intended,
- f. Owing to non-recovery, initiation as to auctioning of the collateral has passed six months and if the recovery process is under litigation,
- g. Loan provided to the borrowers included in the blacklist of credit information center (CIC),

- h. Project or business is not in operative conditions, project or business is not in operation,
- i. Credit Card Loan is not written off within 90 days from past due date.

4. Additional Arrangements in Respects of Term Loan: In respect of term loans, the classification shall be made against the entire outstanding loan on the basis of the past due period of overdue installment.

5. Prohibition to Recover Principal and Interest by Overdrawing the Current Account and Exceeding the Overdraft Limit: Principal and interest on loans and advance shall not be recovered by overdrawing the borrower's current account or where overdraft facility has been extended, by overdrawing such limit. However, this arrangement shall not be constructed as prohibitive for recovering the principal and interest by debiting the customers' account. Where a system in the bank exists as to recovery of principal and interest by debiting the customers' account, and recovery is made as such resulting in overdraft, which is not settled within one month, such overdrawn principal amount shall also be liable to be include under the outstanding loan and such loan shall be downgraded by one step from its current classification. In respects if recognition of interest, the same shall be as per the clause relating to income recognition mentioned in directives no 4.

6. Letter of Credit and Guarantees: If letter of credit and guarantees and other contingent liabilities converted into fund based liabilities and have to be paid, in such condition such loan shall be classified as pass loan within 90 days from the date of conversion into fund based. After 90 days such loan shall be classified as loss loan.

7. Rescheduling and Restructuring of the Loan: If the bank is confident on the following bases of written plan of action submitted by borrower, it may

reschedule or restructure the loans and advances. Clear bases of rescheduling or restructuring should be attached with loan files.

- a. If there is proof of adequate documents and collateral security relating to loan.
- b. If the bank is confident in recovery of restructured or rescheduled loans and advances.

In addition to written plan of action for rescheduling or restructuring of loan, payment of at least 25 percent of total accrued interest up to the date of rescheduling of restructuring should have been collected.

8. Loan Loss Provisioning: The loan loss provisioning, on the basis of the outstanding loans and advances and bills purchases classified as per this directives, shall be provided as follows:

<u>Classification of Loan</u>	<u>Loan Loss Provision</u>
Pass loan	1%
Sub-standard loan	25%
Doubtful loan	50%
Loss	100%

2.2 Review of Previous Studies

In this section, the previous studies, related to the loan management, have been reviewed. This section has been divided in two section. The first section review journals and articles and the second sections reviews the Master's Degree thesis.

2.2.1 Review of Journals and Articles

Duchassi, Shawk, and Seagle, (1988), in their well read article, “*A Knowledge-Engineered System for Commercial Loan Decisions*”, have showed Commercial Loan Analysis Support System (CLASS). This article describe an expert system, commercial loan analysis support

system (CLASS) is an expert system designed to evaluate a company's financial posture, recommend commercial loan decision and pertinent components, and document the loan analysis. Like a loan officer, CLASS constitutently synthetics a large number of detailed facts into a loan recommendation.

CLASS has been designed to seek our any potential weakness in the prospective borrower and conduct an extensive detailed analysis of each weakness. Weaknesses may be over analyzed but none will be overlooked. This approach is consistent with the general notion in commercial lending that one is primarily concerned with weaknesses instead of strong points which are taken for granted. In addition to the limited validation conducted by the expert a more comprehensive validation can be implemented in two ways. First, the system can be empirically tasted with a large sample of historical loan decisions. Second field tested can be conducted in which loan officer use CLASS while making actual loan decisions. Their judgments can be compared to those of CLASS at each step in the analysis. By building CLASS, it was demonstrated that financial knowledge can be represented and applied to a complex financial problem. It is hoped that the approached described have will page the way for building expert systems that address other important financial problems.

Srnivasan and Yung, (1988), in their well read article, "*A Case Study of Corporate Credit Management*", explained an expert credit granting system prototype in designing expert financial systems. Credit granting process in the participating corporation considered of two distinct phases (1) a customer evaluation phase, where the customer's credit worthiness is evaluated based on a variety of criteria; and ii) a credit limit determination phase, where the conclusions of the analysis are transformed into a credit limit or the customer. System design was therefore, split into two phase, (i)

development of an appropriate data base and knowledge base to support the customer evaluation process and (ii) development of an appropriate model to support the credit limit determination phase.

This article has assumed to describe an expert credit granting prototype designed for a fortune 500 corporation. The focus has been on the conceptual process undertaken for designing the prototype. The model base and rules that comprise the prototype are combination of normative prescriptions and managerial preferences presented in a user-friendly environment issues that need conscious recognition in implementing such

Expert systems in corporate finance were also brought forth. The progress in computer and information technologies has provided financial researcher an opportunity to affect a transfer of the expertise contained in normative model to practicing managers through the medium of intelligent computer systems. This is a modest attempt to provide a conceptual foundation to this notion and illustrate its feasibility.

Shaw and Gentry, (1988), in their well read article, *“Managing and Recommending Business Loan Evaluation (Marble) System”*, generalized expert system that minimize the lending expertise of several banking and finance professionals. The objectives of MARBLE are to help lending officer, credit analysis, and loan review committees to improve the evaluation of loan applicants and to learn how expert system operate. Based on the knowledge base and the information provided on the loan applicant, MARBLE synthesizes the information and estimates the likelihood that the loan will be repaid. Knowing that the conclusion recommended by MARBLE reflects the judgments of lending experts, management can use it to assist in the lending decision. The MARBLE system has the capability of learning from decision examples. Examples were used to show the value of inductive inference in the knowledge acquisition process. This learning capability

makes it possible to build an intelligent decision support system. An empirical study shows encouraging result for incorporating inductive learning in MARBLE for loan evaluation.

Keith, (1999), in his well read article, “*An Evaluation of Bank Credit Policies for Farm Loan Portfolios using the Simulation Approach*”, stated that when many borrowers are combined to form a portfolio, borrowers may be graded on a common basis through the expected loss spectrum for default risk and security risk using a two-dimensional risk classification matrix structure. The extent to which unexpected losses on individual loan securities are correlated defines systematic risk while the remaining portfolio risk constitutes unsystematic risk. Systematic risk among loan securities occurs as a result of correlation of loss probabilities between different types of borrowers. Since the probability of default of borrowers is directly related to their income distributions, correlations of loss distributions occurs as a result of a common set of exogenous factors affecting income distributions of borrowers in different regions and industries. Beta risk on loan securities is therefore assessed on the basis of securities classified for regional and industry segmentations.

Koirala, (2006), in his well read article, “*Credit Culture of Commercial Banks in Nepal*”, has concluded that the unorganized moneylenders in Nepal never loose. They used to assess the record of accomplishment of potential borrowers and innocent characters termed as the best borrower. The bank, on the other hand, is an institution established to support and improves development process of a nation. The politicians and the staff have been responsible for the existence of huge volume of NPA in state-owned commercial banks. In order to improve the situation, there is a need to evolve a more acceptable working system backed by cooperation and realization by the banks employees as well as the politicians and stakeholders, who can influence in banks operation.

Garg, (2006), in his well read article, *“Principles of Lending and Credit Culture at Rastriya Banijya Bank”*, has concluded that banks credit culture is the unique combination of policies, practices, experience, and management attitudes that defines the lending environment and determines the lending behavior acceptable to the bank. Loans are not be made unless there is a demonstrated capability for repayment. Lending culture can take cash flows as opposed to security. Every credit must be subject to rigorous analytical scrutiny of the customer’s repayment capability prior to approval, and on an ongoing basis following approval. There can be no exceptions to the basics principles of lending.

Dhungana, (2006), in his well article, *“Problems of NPL’s and the Need of Financial Discipline in the Nepalese Banking System”*, has concluded that poor credit management and deterioration in the quality of loans give birth to non-performing assets. The internal measures play significance role to control the growth of NPL. 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 are accurately identified, assessed and controlled properly. A proper risk management is undoubtedly an important tool for a good banking and NPL management.

He further states that it can be expected that the financial sector reforms will lower down the level of NPL from the existing level and strengthening the banks and financial institution internally to manage the credit portfolio efficiently and support will be continued to make a good credit culture in the system.

Bhandari, (2007), in his well read article, *“Etiology and Strategy of Loan Repayment”*, has concluded that lending agencies should adopt several

strategies for achieving their target of credit repayment. However, before enforcing coercive actions against entrepreneur and the enterprise, the banks and the lending agencies should follow a series of liberal strategies for recovering their loans.

Zerith (2008), in her article well read article, "*Loan Portfolio Management*", affirmed that to manage the loan portfolios, bankers must understand not only the risk posed by each credit but also how the risks of individual loans and portfolios are interrelated. These interrelationships can multiply risk many times beyond what it would be if the risks were not related. Until recently, few banks used modern portfolio management concepts to control credit risk. Now, many banks view the loan portfolio in its segments and as a whole and consider the relationships among portfolio segments as well as among loans. These practices provide management with a more complete picture of the bank's credit risk profile and with more tools to analyze and control the risk.

Zerith further concluded that effective loan portfolio management begins with oversight of the risk in individual loans. Prudent risk selection is vital to maintaining favorable loan quality. Therefore, the historical emphasis on controlling the quality of individual loan approvals and managing the performance of loans continues to be essential. But better technology and information systems have opened the door to better management methods. A portfolio manager can now obtain early indications of increasing risk by taking a more comprehensive view of the loan portfolio.

2.2.2 Review of Thesis

Banstala (2003), in his Master's thesis, "*Loan Disbursement and Repayment Pattern of Agricultural Development Bank of Nepal*", has the main objective to examine the situation of loan disbursement and repayment in ADBL. The specific objectives of the research are;

- a. To analyze the relationship between loan disbursement and loan repayment.

- b. To analyze the relationship between loan disbursement and outstanding loan.
- c. To predict the values of loan disbursement, loan repayment and outstanding loan for the next five years.

The major findings of the study are;

- a. Repayment loan of Bank seems to be directly proportional to the loan disbursement because both have shown movement in same direction i.e. there was increasing order.
- b. Outstanding loan of the banks seems to be directly proportional to the loan disbursement. Because both have shown movement in same direction i.e. there was increasing order.
- c. The amount of the bank's loan disbursement is largely dependent upon the amount of loan repayment in each year.

Pathak (2004), in this Master's thesis, "*Loan Investment and Collection Analysis of Development Banking of Agricultural Development Bank Nepal*", has the main objective to analyze the loan investment and collection of ADBL.

The specific objectives of the study are;

- a. To examine the achievement of purpose wise, term wise and development region wise loan investment, collection and outstanding.
- b. To predict the value of loan investment and collection for 2003/04 to 2007/08.
- c. To examine the impact of last ten years' political insurgency and instability to farmer and ADBL with special reference to loan investment collection and outstanding.

The major findings of the study are;

- a. The actual loan investment and collection is in an increasing ratio and weighted growth rate is in a fluctuating trend.
- b. The agricultural sector required more investment the other sector.

- c. ADBL has to invest continue in current profitable purpose, revise unprofitable purpose.
- d. ADBL has to identify other possible line of agricultural opportunities as well as should create portfolios on different purpose to be operationally and economically viable.

Thapa (2005), in his Master's thesis, "*Lending Policy of Commercial Banks in Nepal*", has the objective to provide the lending practices in NIBL and SBI bank. The specific objectives are;

- a. To examine the liquidity and assets management of NIBL and SBI.
- b. To evaluate the investment policy of NIBL and SBI.
- c. To study the growth ratio of loan and advances.
- d. To analyze the investment to total deposit and net profit NIBL and SBI.

The major findings of the study are;

- a. Both banks current assets have exceeded the current liabilities therefore the ratio is considered satisfactory. But the cash reserve ratios have fluctuated in high degree.
- b. NIBL has maintained both current ratio and cash reserve ratio better than that of SBI.
- c. The assets management ratio shows that deposit utilization of NIBL is less effective than SBI.
- d. NIBL has invested lower amount of government securities and share and debenture than that of NIBL.
- e. The growth ratio of total deposit, loan and advances, total investment and net profit of NIBL are less than that of SBI.

Pyakurel (2006), in his Master's thesis, "*Loan Disbursement and Recovery of Nepal Bank Limited*", has the main objectives to examine the loan management in NBL. The other specific objectives are;

- a. To examine the loan disbursement process.
- b. To analyze the condition of loan recovery.

- c. To examine the efficiency of new management on recovery of loan.

The major findings of the study are;

- a. The present disbursement and recovery of NBL is normal. It is able to recover due loan unexpected.
- b. The conflict of nation forced the bank to reduce many branches and thus the bank can not disburse additional loan in priority sector.
- c. The new management of NBL is not only effective for collecting over due loan, but also effective for managing every essential factors of bank.
- d. The bank faced a lot of fraud by bad-employee in case of loan disbursement, recovery and expenses.
- e. The system is not strict, effective and efficient. Loan has not been provided with technical facility. Geographical features and infrastructure development of the country have not been considered while making policy.

Tamrakar (2006), in his Master's thesis, "*Study on Loan and Advances of Commercial Banks; with Special Reference to NIBL, EBL and NIC*", has the main objective to present the loan and advance situation in NIBL, EBL and NIC. The specific objectives are;

- a. To examine the present situation of loans and advances made by the commercial banks.
- b. To evaluate facts regarding the lending and recovery of loans.
- c. To analyze the lending capacity of the banks.
- d. To assess the current situation of NPA in commercial banks and analyze its effect on the performance of commercial banks.

The major findings of the study are;

- a. The analysis of classified form of non-performing loan shows the amount of doubtful loan of NIBL is higher than substandard loan. Out of total non-performing loan of NIBL, more than 50% is bad loan. EBL

fails to maintain volume of substandard and doubtful loan higher than bad loan and in last year almost all the substandard and doubtful loan turns to bad loan i.e. around 95%. Most of the non-performing loan of NIC is substandard.

- b. The average amount of interest suspense of NIBL is 46.03 million, EBL is 32.41 million and NIC is 15.99 million.
- c. The analysis of loan & advances to total assets ratio reveals that portion of loan & advances in total assets of NIBL is fluctuating while that of EBL and NIC is increasing, however there is certain exceptions. The average ratio of NIBL is 56.76% and that of NIC is 55.96% just behind NIBL and that of EBL is highest at 63.03%.
- d. The maximum percent of deposit invested in loan & advance by NIBL is 75% in 2059/60, however the mean ratio is 67.21% and the average of NIC is also almost equal at 67.65%. In case of EBL, the ratio of loan & advances to total deposit ratio is consistent through out the period around 74%, except in 2057/58 where it was only 66%.
- e. All three banks believe in providing loan to private sector, as private sector loan is more profitable than other. The average private sector loan in total loan of NIBL is 96.96%. The average of EBL is just higher than that at 98.87% while that of NIC is just below that at 93.67%.

K.C. (2007), in his Maser's thesis, "*Loan Disbursement and Collection Procedures of Agriculture Development Bank Ltd.*", has the objective of examining the loan disbursement procedure, evaluate the trend of loan investment and collection and analyze the relationship between targeted and actual investment and collection of ADBL.

The major findings of the study are;

- a. Targeted loan investment and collection has increased every year and weight age growth rates are in fluctuating trend. Percent of targeted loan collection to investment is in fluctuating trend. This

indicates that there is some error in standard setting.

- b. Actual loan investment and collection has also increased every year. From t-test it is found there is no significant different between targeted/actual loan investment and collection.
- c. Actual loan outstanding has incased every year and the weight age growth rate is in fluctuating trend. The highest % of collection to outstanding is 53.37% in F/Y 2062/63. The figure represents that very low % of collection to outstanding ratio.
- d. ADBL is often less than fully effective in collecting all available information, or in considering later how it could improve its methods of evaluating clients. In addition, there is a serious difficulty in sharing information about borrowers among bankers and between bankers and other firms.

Sharma (2008), in his Master's thesis, "*A Study on Loan Management of Agriculture Development Bank Limited*" has the main objective to evaluate the loan disbursement and collection procedure of ADBL. In accordance to this main objective the study has other specific objectives;

- a. To examine the loan disbursement and collection procedure of ADBL.
- b. To evaluate the trend of loan investment, collection and outstanding.
- c. To show the achievement of purpose-wise and term-wise loan disbursement, outstanding and collection of ADBL.
- d. To study lending policy, loan recovery procedure, interest rate and discount of ADBL.

The major findings of the study are;

- a. The total investment of development financing increased from Rs. 7.13 billion in FY 057/58 to Rs. 12.85 billion in FY 063/64 registering an annual average growth trend of Rs.0.82 billion or 10.43%.
- b. The total collection of development financing increased from Rs. 5.34 billion in FY 057/58 to Rs. 11.84 billion in FY 063/64 registering an

- annual average growth trend of Rs. 0.93 billion or 14.22%.
- c. The total outstanding of development financing increased from Rs. 12.89 billion in FY 057/58 to Rs. 22.18 billion in FY 063/64 registering an annual average growth trend of Rs. 1.33 billion or 9.53%.
 - d. Actual loan investment/disbursement, collection and outstanding of short-term is gradually increased every year. The lowest percentage of loan collection to disbursement is 76.46% in FY 060/61 and the highest is 87.33% in FY 063/64.

2.3 Research Gap

Rastriya Baniya bank is the second commercial bank of Nepal and thus has significant contribution to increase the revenue of the government and to buttress the national economy. As a result, the smooth operation of RBB is crucial. For such, RBB should have sound earning capacity. Since, interest income from loan is the major source of income of each commercial bank, a bank should be perfect in managing loan. All of the above researches mainly concentrate on secondary data and thus ignore the primary data, which could enhance the banking performance. Thus to fulfill such gap, the present study embraces both the primary and secondary data. Further, the study makes relationship of loan and advances with other financial indicators and makes trend analysis of loan and advances and others for the next four fiscal year periods.

CHAPTER - III

RESEARCH METHODOLOGY

This chapter is related to the research methodology employed in the entire aspect of the study. Research methodology is a way to systematically solve the problem. In it the various steps that are generally adopted in achieving the objectives of the study are stated.

3.1 Research Design

Research design is the plan, structure and strategy of investigation conceived so as to obtain answers to research questions and to control variance. The plan is the overall scheme or program of research. It includes an outline of what the investigator will do from writing the hypothesis and their operational implications to the final analysis of data.

Being an academic research, the purpose of this research is to answer the queries raised and control the variances. Analytical and descriptive research design, a fact finding approach, is followed for accessing the loan management of RBB. Regression analysis and coefficient of correlation techniques are applied for determining the relationship between the figures of loan and net profit.

3.2 Population and Sample

There exist 26 commercial banks operating in Nepal, which are assumed to be the population of the study. But, is not possible to study all of these commercial banks within this study. So taking the total number of commercial banks as population of the study, only one commercial bank, namely Rastriya Banijya Bank (RBB) has been taken as sample.

3.3 Nature and Sources of Data

To fulfill the predetermined objectives that are set up for the study, both primary and secondary sources are included. The secondary data have been obtained from mainly the annual report of RBB. Further, brochures, Souvenir, and the official website have also been extensively used to collect the secondary data. However, the primary data have been collected through making questionnaire containing 10 questions, and distributing it to the respondents. Apart from above mentioned sources, relevant data are collected from;

- a. Economic surveys of various years, published Ministry of Finance, Government of Nepal.
- b. Statistical records gathered from Central Bureau of Statistics.
- c. Banking and Financial Statistics published by Nepal Rastra Bank.
- d. Periodicals, bulletins, magazines and other published and unpublished reports of concerned authorities and research works.

3.4 Tools Used

For the processing of data collected, both the financial and statistical tools have been extremely used.

3.4.1 Financial Tools

Under this mainly the ratio analysis that is relevant to the loan management of the bank has been done.

a) Loan Investment to Loan Outstanding

This ratio measures the relationship between the loan investment per year and the total accumulated loan outstanding. A stable policy of loan investment considering the loan outstanding is crucial for sound loan management.

$$\text{Loan Investment to Loan Outstanding} = \frac{\text{Loan Investment}}{\text{Loan Outstanding}}$$

b) Loan Recovery to Loan Outstanding

This ratio measures the relationship between loan recovery and loan outstanding. The ratio reflects the efficiency of the bank in collecting the loan amount disbursed.

$$\text{Loan Recovery to Loan Outstanding} = \frac{\text{Loan Recovered}}{\text{Loan Outstanding}}$$

c) Growth Ratios

Under this, the growth of loan investment, loan outstanding and the loan recovery of RBB have been calculated. This ratio reflects the status of loan management of the bank.

$$\text{Growth Ratio} = \frac{\text{Current Value} - \text{Previous Value}}{\text{Previous Value}} \times 100$$

d) Non Performing Loan to Total Loan

NRB has directed all the commercial banks create loan loss provision against the doubtful and bad debts. But both of our concerned banks have not provided data on non-performing loan in balance sheet and profit & loss account. Non-performing loans to total loan and advances ratio shows the percentage of non-recovery loans in total loans and advances. This ratio is calculated as:

$$\text{NPL to Total Loan} = \frac{\text{Non Performing Loan}}{\text{Total Loan}}$$

e) Loan Loss Provision to Total Loan

Each bank has to keep the loan loss provision for loan and advances as per the direction of Nepal Rastra Bank. The loan loss provision to total loans and advances measures the aggregate percentage of loan loss provision kept by bank on loans and advances and thus eventually measures the security position.

$$\text{Loan Loss Provision to Total Loan} = \frac{\text{Loan Loss Provision}}{\text{Total Loan}}$$

f) Total Loan to Total Deposit

This ratio is calculated to find out how successfully the banks are

utilizing their deposits on loan and advances for profit generating activities. Greater the ratio indicates the better utilization of total deposits. It is calculated as:

$$\text{Total Loan to Total Deposit ratio} = \frac{\text{Total Loan}}{\text{Total Deposit}}$$

3.4.2 Statistical Tools

The analysis could not have been done without using the statistical tools. The following statistical tools have been effectively utilized for data analysis.

a) Mean

Arithmetic mean or simply a mean of a set observations is the sum of all the observations divided by the number of observations. Arithmetic mean is also known as the arithmetic average.

Let $x_1, x_2, x_3, \dots, x_n$ be the n values of the variable then their arithmetic mean denoted by \bar{x} is defined by,

$$\bar{x} = \frac{x_1 + x_2 + x_3 + \dots + x_n}{n}$$

Where, n is the number of observations.

b) Standard Deviation

The standard deviation is the absolute measure of dispersion in which the drawbacks present in other measures of dispersion are removed. It is said to be the best measure of dispersion as it satisfies most of the requisites of a good measure of dispersion.

$$\text{s.d.} = \sqrt{\frac{\sum (x - \bar{x})^2}{N}}$$

c) Coefficient of Variation

The coefficient of dispersion based on standard deviation multiplied by 100 is

known as the coefficient of variation (C.V.). Less the C.V., more will be the uniformity and more the C.V., less will be uniformity. If \bar{x} be the arithmetic mean and s.d the standard deviation of the distribution, then the C.V. is defined by,

$$\text{C.V. \%} = \frac{\text{S.D.}}{\text{Mean}} \times 100$$

d) Karl Pearson's Correlation Coefficient

Two values are said to have 'correlation', when they are so related that the change in the value of one variable is accompanied by the change in the value of the other. One of the widely used mathematical methods of calculating the correlation coefficient between two variables is Karl Pearson's correlation coefficient 'r'. It is calculated as;

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

e) Probable Error

The probable error denoted by P.E. is used to measure the reliability and test of significance of correlation coefficient. Significance of relationship has been tested by using the probable error (P.E.) and it is denoted by the following model:

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

Where, r = the value of correlation coefficient

n = number of pairs of observations

if $r < \text{P.E.}$, it is insignificant, i.e. there is no evidence of correlation

if $r > 6 \text{ P.E.}$, it is significant

if $\text{P.E.} < r < 6 \text{ P.E.}$, nothing can be concluded

f) Regression Lines

The regression line is the line that gives the best estimate of one variable for any given value of the other variable. The simple regression equation of dependent variable (Y) on the independent variable (X) is given by;

$$y = a + bx$$

We shall get the normal equation for estimating “a” and “b” as.

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

$$\sum XY = a \sum Y + b \sum Y^2$$

Where,

X = the value of independent variable

Y = the value of dependent variable

a = Y-intercept

b = slope of the trend line/coefficient of regression

N = number of pairs of observations.

$$a = Y - b X$$

g) Trend Analysis

A widely and most commonly used method to describe the trend is the method of least square. Let the trend line between the dependent variable y and the independent variable x (i.e. time) be represented by;

$$Y_c = a + bx \dots\dots\dots (i)$$

Where,

a = y intercept or value of y when x = 0

b = slope of the trend line or amount of change that comes in y of a unit change in x.

To find the value of x and y, the following equations should be solved;

$$\sum y = na + b \sum x \dots\dots\dots (ii)$$

$$\sum xy = a \sum x + b \sum x^2 \dots\dots\dots (iii)$$

CHAPTER – IV

DATA PRESENTATION AND ANALYSIS

This section is the main part of the study and achieves the objectives set out in the first chapter. Further, both the statistical and financial tools stated in the third chapter are efficiently used in this chapter to accomplish the goal of the study. In this chapter, both the primary and secondary data collected have been analyzed and at the findings have been drawn at the end of this section.

4.1 Secondary Data Analysis

In this part of the study, the secondary data that are related to the loan and extracted from mainly the annual reports of the bank have been analyzed. Different ratios that reflect the loan management of RBB has been introduced. Further, the statistical relationship between loan and advances and other major financial indicators have been analyzed. In addition, the values of loan and advances and other have been estimated in the forthcoming four fiscal years.

4.1.1 Loan Investment to Loan Outstanding

This ratio measures the relationship between loan investment with loan outstanding and shows by how much extent the loan outstanding is greater than the loan investment. The ratio also signals the trend of loan investment and loan outstanding. The loan investment to loan outstanding of RBB is presented in the Table 4.1.

Table 4.1
Loan Investment to Loan Outstanding

Previous Five Years				Current Five Years				
FY	LI	LO	Ratio	FY	LI	LO	Ratio	
1999/00	999.97	34744.27	2.88	2004/05	3848.16	27000.93	14.25	
2000/01	8590.17	27375.13	31.38	2005/06	1678.11	23246.51	7.22	
2001/02	3227.86	27037.37	11.94	2006/07	3304.22	24871.36	13.29	
2002/03	446.14	26608.83	1.68	2007/08	4152.28	27524.92	15.09	
2003/04	930.97	25105.68	3.71	2008/09	9539.24	36042.93	26.47	
Mean			10.32	Mean			15.26	
S.D.			11.13	S.D.			6.25	
C.V.%			107.94	C.V.%			40.94	
		Overall Average				12.79		
		S.D.				9.36		
		C.V.%				73.20		

(Source: Appendix II)

The table above showed the status of loan investment and loan outstanding of RBB in two five-fiscal year periods. In the previous five-fiscal years, the ratio of loan investment to loan outstanding was in fluctuating trend. This clearly indicated that the loan investment did not move in the same pace as the loan outstanding did. Clearly, the loan investment of the bank ranged from Rs. 446.14 millions in the fiscal year 2002/03 to Rs. 8590.17 millions in the fiscal year 2000/01 and loan outstanding ranged from Rs. 25105.68 millions in the fiscal year 2003/04 to Rs. 34744.27 millions in the fiscal year 1999/00 within the previous five-fiscal year periods. Unlike loan investment, the loan outstanding followed decreasing trend in the previous five-fiscal year periods, which was a good indication of loan recovery. Consequently, the ratio of loan investment to loan outstanding of the bank was 2.88%, 31.38%, 11.94%, 1.68% and 3.71% in the fiscal year 1999/00, 2000/01, 2001/02, 2002/03 and 2003/04 respectively. In the previous five-fiscal year periods, the average loan

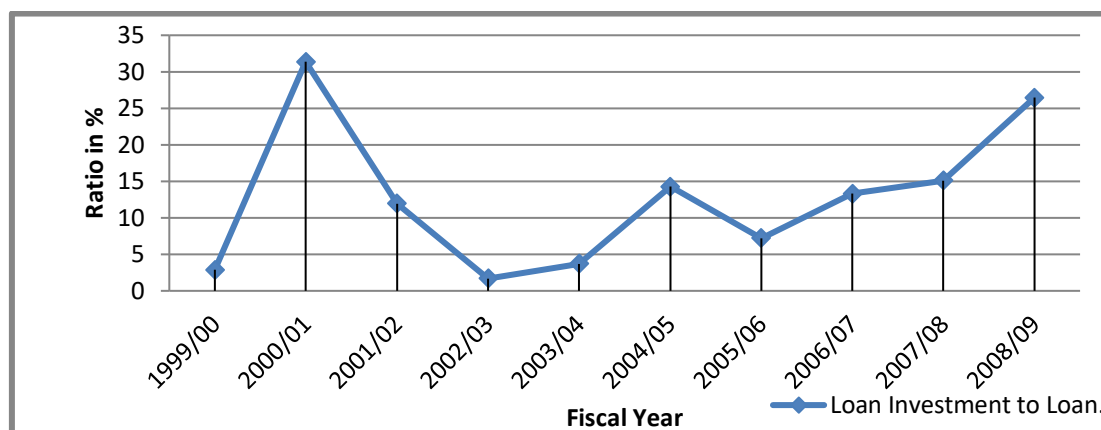
investment to loan outstanding was 10.32% and the coefficient of variation in the ratio was 107.94%, indicating higher inconsistency.

In contrast, the loan investment of RBB in the current five-year periods was found to be in increasing trend, except in the fiscal year 2005/06. Thus, the loan investment ranged from Rs. 1678.11 millions in the fiscal year 2005/06 to Rs. 9539.24 millions in the fiscal year 2008/09. However, the loan outstanding followed fluctuating trend and thus was highest, Rs. 36042.93 millions in the fiscal year 2008/09 within the current five-fiscal year periods. The ratio of loan investment to loan outstanding of RBB within these periods was also found to be in fluctuating trend. The ratio was 14.25%, 7.22%, 13.29%, 15.09% and 26.47% in the fiscal year 2004/05, 2005/06, 2006/07, 2007/08 and 2008/09 respectively. The average ratio within these periods was 15.26% and the coefficient of variation in the ratio was 40.94%.

Comparing two periods, it can be concluded that RBB disbursed more loan in proportion to loan outstanding in the current five years periods than in last five year periods. However, in overall, RBB disbursed 12.79% of the total loan outstanding and the coefficient of variation in the ratio was 73.20%, which indicated higher inconsistency in the ratio. This seemed that RBB lacks appropriate loan investment policy. Thus, a sound credit policy is germane to RBB to prevent the credit risk.

Figure 4.1

Loan Investment to Loan Outstanding



4.1.2 Loan Recovery to Loan Outstanding

The loan recovery to loan investment depicts the amount of the recovery made by the bank out of the total investment made in each fiscal year. This ratio measures the banks' efficiency in collection at speed. The loan recovery to loan investment of RBB is presented in the Table 4.2.

Table 4.2

Loan Recovery to Loan Outstanding

Previous Five Years				Current Five Years				
FY	LR	LO	Ratio	FY	LR	LO	Ratio	
1999/00	2045.23	34744.27	5.89	2004/05	1952.91	27000.93	7.23	
2000/01	1221.03	27375.13	4.46	2005/06	1522.99	23246.51	6.55	
2001/02	3565.62	27037.37	13.19	2006/07	1679.37	24871.36	6.75	
2002/03	874.68	26608.83	3.29	2007/08	1498.72	27524.92	5.44	
2003/04	1192.89	25105.68	4.75	2008/09	1021.23	36042.93	2.83	
Mean			6.31	Mean			5.76	
S.D.			3.53	S.D.			1.58	
C.V.%			55.98	C.V.%			27.38	
		Overall Average				6.04		
		S.D.				2.75		
		C.V.%				45.55		

(Source: Appendix II)

The above table showed the efficiency of bank in recovering loan in proportion to loan outstanding within the two distinct periods. The table depicted that the loan recovered amount of RBB for the previous five year periods was in fluctuating trend. RBB recovered highest amount of Rs. 3565.62 millions in the fiscal year 2001/02 and lowest amount of Rs. 874.68 millions in the fiscal year 2002/03. Alike the loan recovered amount, the ratio of loan recovery to loan outstanding within the previous five year periods was also in fluctuating trend. The ratio was 5.89% in the fiscal year 1999/00, which decreased to 4.46% in the fiscal year 2000/01, then increased to 13.19% in the fiscal year 2001/02, again decreased to 3.29% in the fiscal year 2002/03, and finally increased to 4.75% in the fiscal year 2003/04. In average, the bank recovered 6.71% of the total loan outstanding within these five year periods, and the coefficient of variation in the ratio was 55.98%, indicating inconsistency.

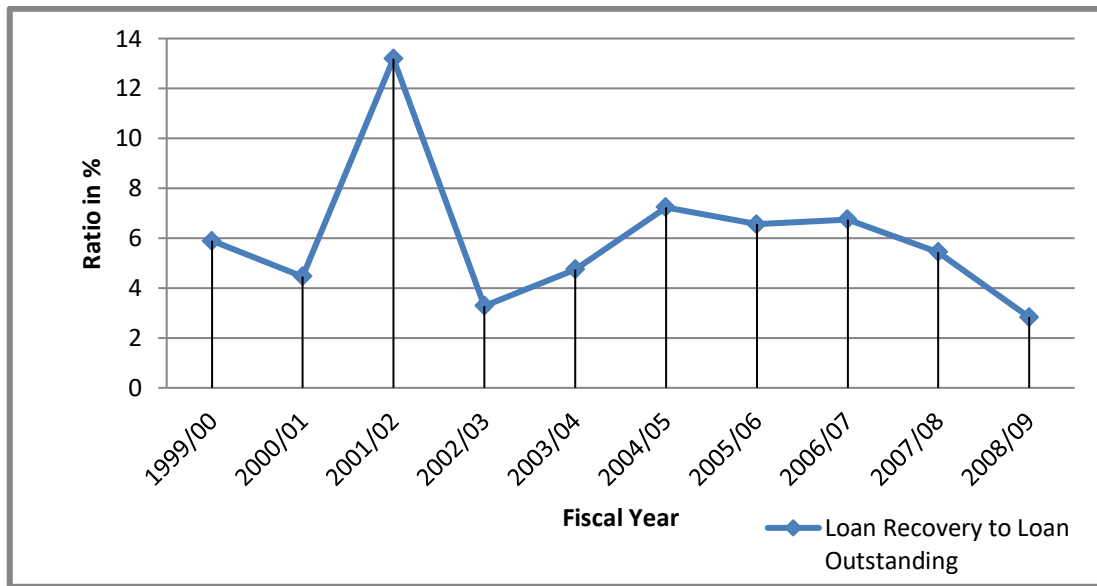
Similarly, the loan recovery amount of RBB in the current five year periods was in decreasing trend, except in the fiscal year 2006/07. RBB recovered Rs. 1952.91 millions, highest, in the fiscal year 1999/00 and Rs. 1021.23 millions, lowest, in the fiscal year 2008/09. Likewise, except in the fiscal year 2006/07, the ratio of loan recovery to loan outstanding of RBB within the current five year periods was in decreasing trend. The ratio was 7.23% in the fiscal year 2004/05, which decreased to 6.55% in the fiscal year 2005/06, then increased to 6.75% in the fiscal year 2006/07, again decreased to 5.44% in the fiscal year 2007/08 and finally reached to 2.83% in the fiscal year 2008/09. In average, the ratio was 5.76%, comparatively lower than the average of one decade, and the coefficient of variation in the ratio was 27.38%.

Comparing two periods, it can be concluded that the loan recovery position of RBB in proportion to loan outstanding was better in the previous five year periods than in current five year periods. However, the loan recovery ratio was not satisfactory. In overall, the bank collected only 6.04% of the total loan

outstanding in the ten year periods, which was quite low. Thus, it is inevitably necessary for the bank to formulate a sound recovery policy.

Figure 4.2

Loan Recovery to Loan Outstanding



4.1.3 Growth Analysis

To know the banks' efficiency in raising loan investment, raising loan recovery and lowering loan outstanding, the growth analysis have been done.

4.1.3.1 Loan Investment Growth

The higher the loan investment made by banks indicates higher interest earning capacity of the bank. So, the higher loan investment is considered better. The growth in loan investment made by RBB has been presented in the Table 4.3.

Table 4.3
Loan Investment Growth

Previous Five Years			Current Five Years		
FY	LI	Growth %	FY	LI	Growth %
1999/00	999.97	35.27	2004/05	3848.16	313.35
2000/01	8590.17	759.04	2005/06	1678.11	-56.39
2001/02	3227.86	-62.42	2006/07	3304.22	96.90
2002/03	446.14	-86.18	2007/08	4152.28	25.67
2003/04	930.97	108.67	2008/09	9539.24	129.73
Mean		150.88	Mean		101.85
S.D.		311.99	S.D.		123.59
C.V.%		206.79	C.V.%		121.35
		Overall Average		126.36	
		S.D.		238.56	
		C.V.%		188.78	

(Source: Appendix II)

The above table showed the loan disbursement growth in two distinct periods and in overall as well. The table depicted that the loan disbursement of RBB was initially Rs. 999.97 millions in the fiscal year 1999/00, which extremely increased by 759.04% in the fiscal year 2000/01 and thus reached to Rs. 8590.17 millions, and then decreased by 62.42% in the fiscal year 2001/02, amounting to Rs. 3227.86 millions, decreased by 86.18% in the fiscal year 2002/03, amounting to Rs. 446.14 millions, and finally increased by 108.67% in the fiscal year 2003/04, amounting to Rs. 930.97 millions, within the previous five year periods. In average, the loan investment of RBB for the previous five year periods rose by 150.88% and the coefficient of variation in the loan investment growth for that period was 206.79%, indicating great inconsistency.

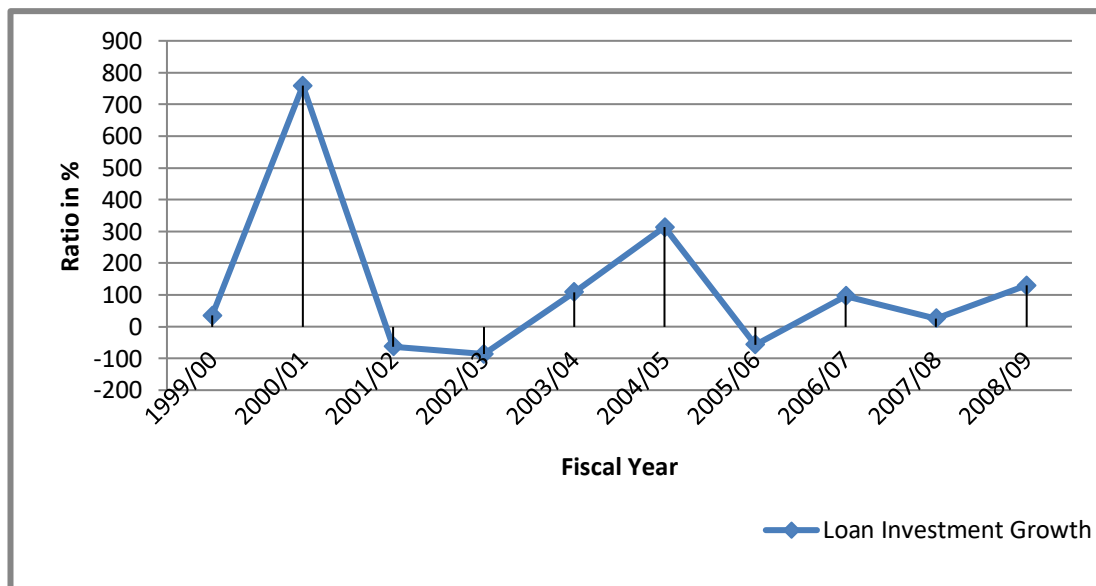
Further, in the current five year periods, the loan investment of RBB followed increasing trend, except in the fiscal year 2005/06. The loan investment of RBB

was Rs. 3848.16 millions in the fiscal year 2004/05, which decreased by 56.39% in the fiscal year 2005/06, and thus amounted to Rs. 1678.11 millions, and then increased by 96.90% in the fiscal year 2006/07, amounting Rs. 3304.22 millions, again increased by 25.67% in the fiscal year 2007/08, amounting Rs. 4152.67 millions, and finally increased by 129.73% in the fiscal year 2008/09, amounting Rs. 9539.34 millions. Thus, the loan investment growth was highest in the fiscal year 2004/05 and lowest in the fiscal year 2005/06. In average, the loan investment of RBB grew by 101.85% within the current five year periods.

Comparing the two distinct periods, it can be concluded that the growth of loan investment was greater in previous five year periods than in current five year periods. In overall, the loan investment of bank grew by 126.36% within the ten year periods, and the coefficient of variation in the growth was 188.28%. It would have been better if the bank had considered the greater chances of earning high interest along with the increment in loan investment.

Figure 4.3

Loan Investment Growth



4.1.3.2 Loan Outstanding Growth

The higher loan outstanding means higher possibility of turning bank loan into bad debt and the inefficiency of bank in recovering loan in time. So, lower the outstanding lower will be the risk of bad debt. The loan outstanding growth of RBB is presented in Table 4.4.

Table 4.4
Loan Outstanding Growth

Previous Five Years			Current Five Years		
FY	LO	Growth %	FY	LO	Growth %
1999/00	34744.27	21.77	2004/05	27000.93	7.55
2000/01	27375.13	-21.21	2005/06	23246.51	-13.90
2001/02	27037.37	-1.23	2006/07	24871.36	6.99
2002/03	26608.83	-1.58	2007/08	27524.92	10.67
2003/04	25105.68	-5.65	2008/09	36042.93	30.95
Mean		-1.58	Mean		8.45
S.D.		13.76	S.D.		14.24
C.V.%		-870.00	C.V.%		168.51
		Overall Average		3.44	
		S.D.		14.87	
		C.V.%		432.90	

(Source: Appendix II)

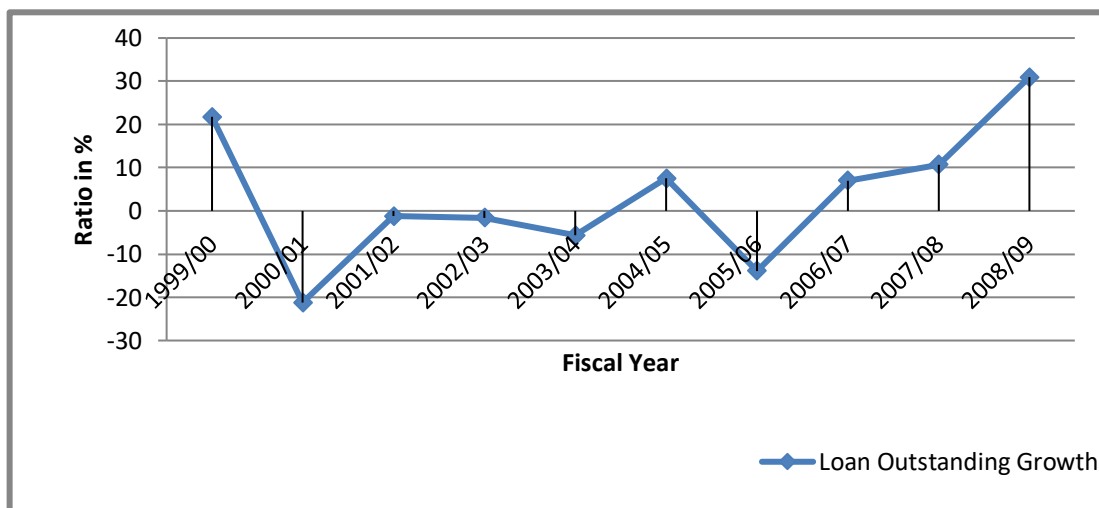
The above table showed the growth of loan outstanding in RBB for the ten year periods. For the first five year periods, the loan outstanding growth of RBB was in decreasing trend, which is quite satisfactory. The loan outstanding of the bank was Rs. 34744.27 millions in the fiscal year 1999/00, which decreased by 21.21% in the fiscal year 2000/01, again decreased by 1.23% in the fiscal year 2001/02, 1.58% in the fiscal year 2002/03 and by 5.65% in the fiscal year 2003/04. The table depicted that the loan outstanding of RBB decreased by 1.58%, which is quite low although good, within the first five fiscal years, and the coefficient of variation in such decrement was 870.00%.

In contrast, the loan outstanding of RBB was in almost in increasing trend, except in the fiscal year 2005/06, within the current five year periods. The loan outstanding ranged from Rs. 27000.93 millions in the fiscal year 2004/05 to Rs. 36042.93 millions in the fiscal year 2008/09. The growth of loan outstanding in

the current five year periods was 7.55%, -13.90%, 6.99%, 10.67% and 30.95% in the fiscal year 2004/05, 2005/06, 2006/07, 2007/08 and 2008/09 respectively. In average, the loan outstanding of RBB increased by 8.45%, indicating inefficiency of the bank in recovering loan, within the current five year periods, and the coefficient of variation in the increment was 168.51%.

Comparing the two distinct periods on the basis of loan outstanding growth, it can be concluded that the previous five year periods was superior to the current five year periods, since the bank was able to decrease the loan outstanding in that periods. However, the loan outstanding of the bank increased only by 3.44% within the ten year periods. Thus, the bank needs to have sound recovery policy to decrease the outstanding loan and increase the loan investment.

Figure 4.4
Loan Outstanding Growth



4.1.3.3 Loan Recovery Growth

The duty of bank does not end only by disbursing loan. The bank should do equal exercise in loan recovery and reduce the chances of bad debt. The higher loan recovery indicates higher efficiency on bank in loan management. The growth in loan recovery of RBB taken for study for the ten year periods is presented in the Table 4.5.

Table 4.5
Loan Recovery Growth

Previous Five Years			Current Five Years		
FY	LR	Growth %	FY	LR	Growth %
1999/00	2045.23	-55.84	2004/05	1952.91	63.71
2000/01	1221.03	-40.30	2005/06	1522.99	-22.01
2001/02	3565.62	192.02	2006/07	1679.37	10.27
2002/03	874.68	-75.47	2007/08	1498.72	-10.76
2003/04	1192.89	36.38	2008/09	1021.23	-31.86
Mean		11.36	Mean		1.87
S.D.		97.97	S.D.		33.95
C.V.%		862.51	C.V.%		1815.59
		Overall Average		6.61	
		S.D.		73.47	
		C.V.%		1110.79	

(Source: Appendix II)

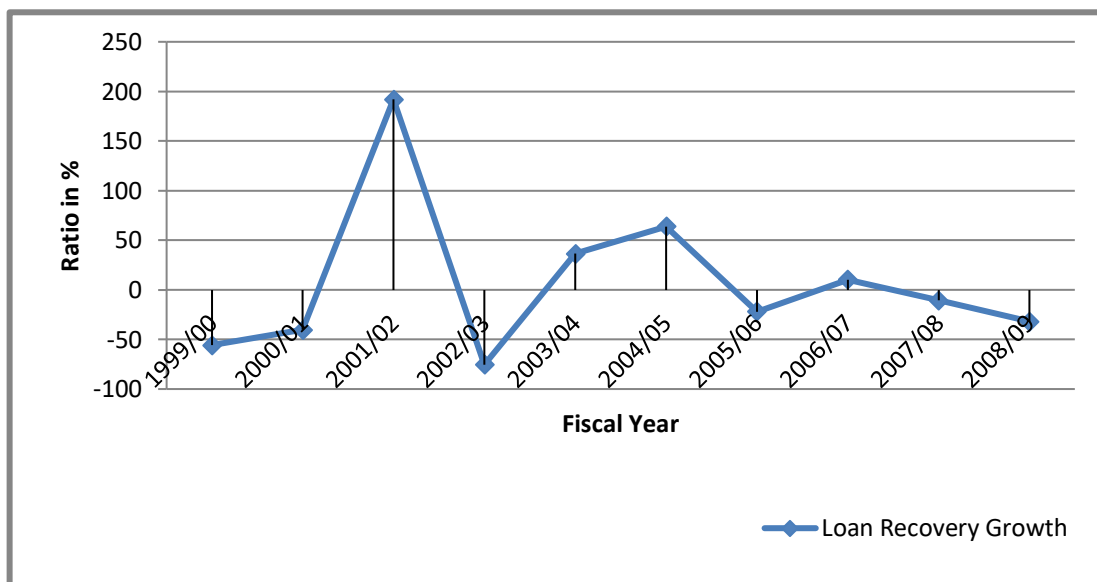
The above table showed the efficiency of RBB in recovering the disbursed loan. For the first five year periods the loan recovery amount was highest, Rs. 3565.62 millions, in the fiscal year 2001/02, and lowest, Rs. 874.68 millions, in the fiscal year 2002/03. The growth rate of recovered loan amount was not in uniform. The loan recovery decreased by 40.30% in the fiscal year 2000/01, and then drastically increased by 192.02% in the fiscal year 2001/02, again decreased by 75.47% in the fiscal year 2002/03 and finally increased by 36.36% in the fiscal year 2003/04. In average, the loan recovery for the first five years of RBB grew by 11.36%, which is quite satisfactory, but the bank should also considered that in most of the year the loan recovery was lower than amount collected in previous year.

Similarly, the loan recovery amount for the current five year periods ranged from Rs. 1021.23 millions in the fiscal year 2008/09 to Rs. 1952.91 millions in the fiscal year 2004/05. Except in the fiscal year 2006/07, the loan recovery amount was in decreasing trend; as a result, the growth rate of loan recovery was also in negative. The loan recovery growth was 63.71%, -22.01%, 10.27%, -10.76% and -31.86% in the fiscal year 2004/05, 2005/06, 2006/07, 2007/08

and 2008/09 respectively. Within these periods, the average collection growth was 1.87%, which was far lower than the previous five year periods.

Comparing the two distinct periods, it can be concluded that RBB was more success in recovering the disbursed loan in the first five year periods than in the current five year periods. However, in both the periods, the recovery growth was quite low. Consequently, the average growth rate of loan recovery for the ten year periods was 6.61% and the coefficient of variation was 1110.79%, indicating extreme inconsistency. Thus, it implies that RBB needs a strong collection policy.

Figure 4.5
Loan Recovery Growth



4.1.4 Non-Performing Loan Analysis

Bad debt and non-performing loan do not have same meaning. They have some fundamental differences in their meaning. Non-performing loan can be debt but debt can not be non-performing loan. Non-performing loan represents the loan that remained unpaid after loan due date. Greater the loan performing loan, the greater will be the credit risk.

4.1.4.1 Non Performing Loan to Total Loan

The non performing loan to total loan measures the credit risk of the bank. Higher the ratio indicates high coverage of non performing loan on total loan and thus indicates high credit risk, which may jeopardize the sustainability of the bank.

Table 4.6
Non Performing Loan to Total Loan

Previous Five Years				Current Five Years			
FY	NPL	LA	Ratio	FY	NPL	LA	Ratio
1999/00	13661.45	34744.27	39.32	2004/05	13689.47	27000.93	50.70
2000/01	12209.31	27375.13	44.60	2005/06	8622.13	23246.51	37.09
2001/02	14889.48	27037.37	55.07	2006/07	7120.67	24871.36	28.63
2002/03	16005.21	26608.83	60.15	2007/08	5953.64	27524.92	21.63
2003/04	14470.91	25105.68	57.64	2008/09	5651.53	36042.93	15.68
Mean			51.36	Mean			30.75
S.D.			8.01	S.D.			12.27
C.V.%			15.60	C.V.%			39.91
		Overall Average			41.05		
		S.D.			14.62		
		C.V.%			35.60		

(Source: Appendix II)

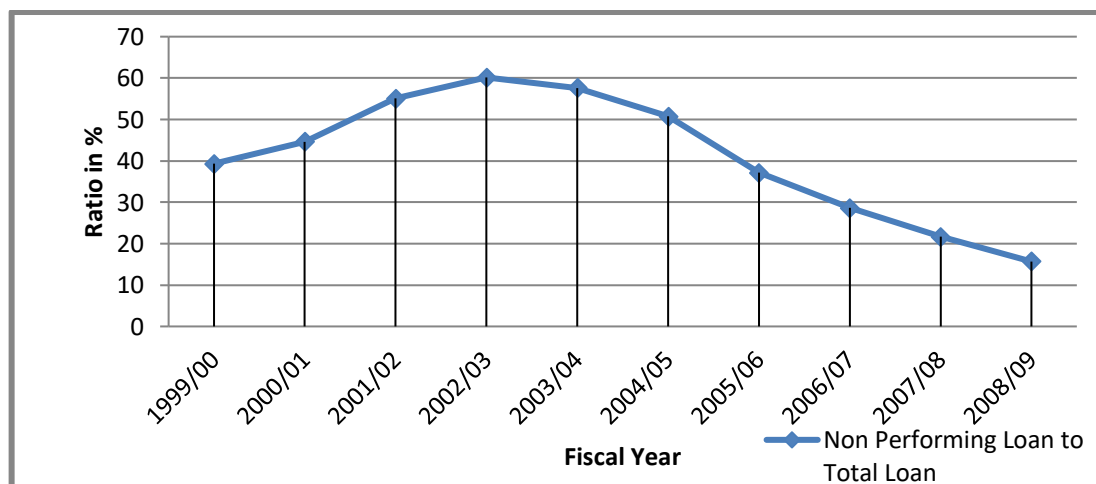
The above table depicted the ratio of non performing loan to total loan to measure the loan situation of RBB. The table showed that the non-performing loan of RBB for the first five year periods was in fluctuating trend and thus ranged from Rs. 12209.31 millions in the fiscal year 2000/01 to Rs. 16005.21 millions in the fiscal year 2002/03. However, the ratio of non performing loan to total was in increasing trend for the first four years. The ratio was 39.32% in the fiscal year 1999/00, 44.60% in the fiscal year 2000/01, 55.07% in the fiscal year 2001/02, 60.15% in the fiscal year 2002/03 and 57.64% in the fiscal year 2003/04. From this it can be inferred that the portion of performing loan was in decreasing trend and thus the loan of RBB is aggravating. In average, the non performing loan covered 51.36% of the total loan, which indicated greater risk in the loan.

In contrast, the ratio of non performing loan to total loan of for the current five year periods of RBB was in decreasing trend, which was quite good. The non performing loan, along with the ratio of non performing loan to total, also followed decreasing trend and thus decreased to Rs. 5651.53 millions in the fiscal year 2008/09 from Rs. 13689.47 millions in the fiscal year 2004/05. Further, the ratio of non performing loan to total loan of RBB was 50.70%, 37.09%, 28.63%, 21.63% and 15.68% in the fiscal year 2004/05, 2005/06, 2006/07, 2007/08 and 2008/09 respectively. The decreasing trend of both the non performing amount and ratio indicated an enhancement in the lending procedures of RBB in the current five year periods. In average, the non performing loan represented only 30.75% of the total loan.

Comparing the two periods, it can be concluded that the lower portion of the loan turned to non performing loan in the current five year periods than in the previous five year periods. Hence, RBB ameliorated the composition of loan. In average, the non performing loan represented 41.05% of the total loan in the ten year periods, indicating that the total loan of RBB was dominated by performing loan.

Figure 4.6

Non Performing Loan to Total Loan



4.1.4.2 Loan Loss Provision to Total Loan and Advances Ratio

As per the NRB directives, each commercial bank has to keep 1% of the performing loan, 25% of the sub-standard loan, 50% of the doubtful loan and 100% of the loss loan as loan loss provision. This loan loss provision to total loan and advances measures the credit risk of the bank. The higher the ratio, the greater will be the credit risk.

Table 4.7

Loan Loss Provision to Total Loan and Advances Ratio

Previous Five Years				Current Five Years			
FY	LLP	LA	Ratio	FY	LLP	LA	Ratio
1999/00	6542.75	34744.27	18.83	2004/05	13570.00	27000.93	50.26
2000/01	7576.85	27375.13	27.68	2005/06	8612.96	23246.51	37.05
2001/02	13347.62	27037.37	49.37	2006/07	7542.63	24871.36	30.33
2002/03	14929.34	26608.83	56.11	2007/08	7709.00	27524.92	28.01
2003/04	14274.59	25105.68	56.86	2008/09	4435.97	36042.93	12.31
Mean			41.77	Mean			31.59
S.D.			15.59	S.D.			12.37
C.V.%			37.33	C.V.%			39.14
		Overall Average			36.68		
		S.D.			14.96		
		C.V.%			40.80		

(Source: Appendix II)

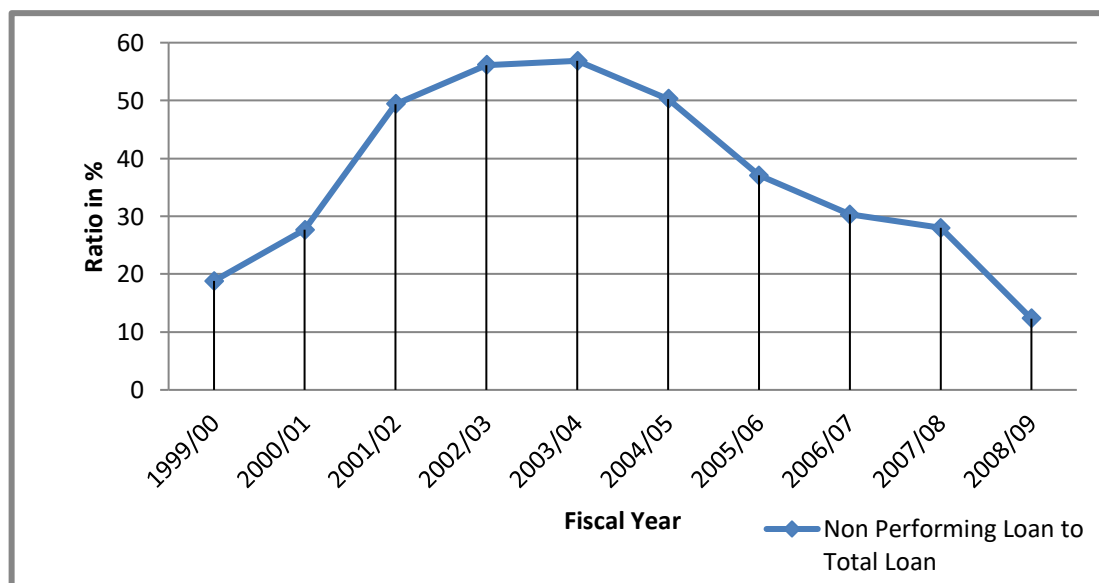
The above table measured the credit risk of RBB. The table showed that the loan loss provision kept in proportion to total loan and advance within the first five years periods was in increasing trend. Clearly, the conversion of sub standard loan and doubtful loan to loss loan was in increment within this period. The loan loss provision to total loan of RBB was 18.83%, 27.68%, 49.37%, 56.11% and 56.86% in the fiscal year 1999/00, 2000/01, 2001/02, 2002/03 and 2003/04 respectively. In average, RBB kept 41.77% of the total loan as loan loss provision within the first five year periods. And the loan loss provision amount in this period ranged from Rs. 6542.75 millions in the fiscal year 1999/00 to Rs. 14929.34 millions in the fiscal year 2002/03.

In contrast, the loan loss provision to total loan in the current five year periods of RBB followed decreasing trend, which indicated the proportion of performing loan, sub standard loan and doubtful loan were in increasing trend, and thus lowering the chances of default loan. Further, the loan loss provision amount ranged from Rs. 13570.00 millions in the fiscal year 2004/05 to Rs. 4435.97 millions 2008/09. The loan loss provision to total loan was 50.26%, 37.05%, 30.33%, 28.01% and 12.31% in the fiscal year 2004/05, 2005/06, 2006/07, 2007/08 and 2008/09 respectively. And the average ratio within this period was 31.59%, and the coefficient of variation was 39.14%.

Comparing two periods, it can be concluded that the credit risk of RBB was lower in the current period in comparison to that in the previous periods. Yet, the average loan loss provision to total loan of RBB for the ten year periods was 36.68%, and the coefficient of variation in such period was 40.80%. It would be worthwhile, if RBB adopts sound credit policy to reduce the loss loan and to convert non performing loan to performing loan.

Figure 4.7

Loan Loss Provision to Total Loan and Advances Ratio



4.1.5 Deposit Mobilization on Loan and Advances

Loan and advances is considered as the major source of income of the bank. The greater the bank invests the funds in loan and advances, the higher will be the chance of earning interest, if the credit risk is low. Thus, to examine the mobilization rate of collected deposit in loan and advances the ratio has been calculated.

Table 4.8
Loan and Advances to Total Deposit

Previous Five Years				Current Five Years				
FY	LA	TD	Ratio	FY	LA	TD	Ratio	
1999/00	34744.27	38575.14	90.07	2004/05	27000.93	43016.06	62.77	
2000/01	27375.13	40773.66	67.14	2005/06	23246.51	46195.48	50.32	
2001/02	27037.37	38993.29	69.34	2006/07	24871.36	50464.13	49.29	
2002/03	26608.83	39402.27	67.53	2007/08	27524.92	57970.85	47.48	
2003/04	25105.68	40866.77	61.43	2008/09	36042.93	68095.70	52.93	
Mean			71.10	Mean			62.77	
S.D.			9.85	S.D.			50.32	
C.V.%			13.85	C.V.%			49.29	
		Overall Average				61.83		
		S.D.				12.21		
		C.V.%				19.75		

(Source: Appendix II)

The above table measured the mobilization of total deposit in loan and advances. The table showed that for the first five years period, the loan and advances was in decreasing trend and the total deposit collection was in increasing trend, except in the fiscal year 2000/01. The deposit collection amount ranged from Rs. 38575.14 millions in the fiscal year 1999/00 to Rs. 40866.77 millions in the fiscal year 2003/04. However, the mobilization of deposit in loan and advances of the bank had remained volatile. The total loan and advances to total deposit of RBB in such period was 90.07%, 67.14%, 69.34%, 67.53% and 61.43% in the fiscal year 1999/00, 2000/01, 2001/02, 2002/03 and 2003/04 respectively. In average, RBB mobilized 71.10% of the

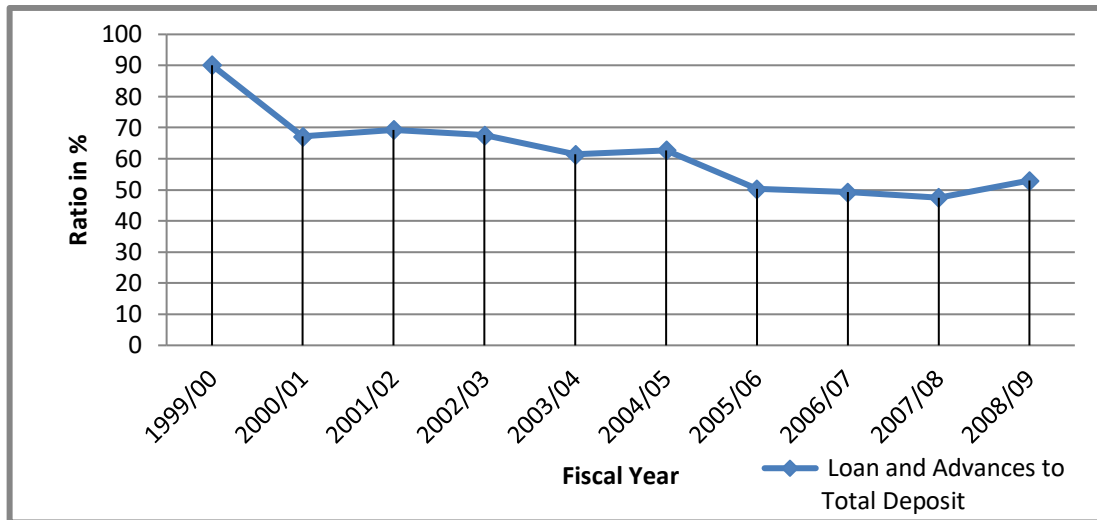
total collected deposit in granting loan and advances. Also, the coefficient of variation in the ratio in the first five year period was 13.85%, indicating quite uniformity in the ratio.

However, the mobilization rate of total deposit in loan and advances decreased for the first four years of the current five year periods, although the deposit collection amount was in increasing trend, ranging from Rs. 43016.06 millions in the fiscal year 2004/05 to Rs. 68095.70 millions in the fiscal year 2008/09. The mobilization ratio was 62.77% in the fiscal year 2004/05, 50.32% in the fiscal year 2005/06, 49.29% in the fiscal year 2006/07, 47.48% in the fiscal year 2007/08 and 52.93% in the fiscal year 2008/09. The lower ratio compared to the previous fiscal year indicated that the bank gave more consideration to other investment sectors. However, the coverage of loan and advances on total deposit was significant. As a result, RBB mobilized 62.77% of the total deposit in disbursing loan.

Comparing to two distinct periods, it can be concluded that the deposit mobilization rate of RBB in loan and advances was more in previous five year period than in the current five year period. Further in average, RBB utilized 61.83% of the total deposit in granting loans, and the coefficient of variation in the ratio was only 19.75%. Thus, loan and advances was the major use of deposit collection than other investment.

Figure 4.8

Loan and Advances to Total Deposit



4.1.6 Statistical Analysis

In this part of the study, the simple correlation and regression analysis, and the trend value of variables, which reflect the loan management of the bank, have been determined.

4.1.6.1 Correlation Analysis

To investigate the synchronization of loan & advances with net profit, with total deposit, with total investment, and with non performing loan, the Karl Pearson’s correlation coefficient (r) has been determined.

4.1.6.1.1 Correlation Analysis between Net Profit & Loan and advances

To determine the relationship between net profit and loan and advances, the correlation between them has been calculated. Further, the relationship derived has been tested by using probable error.

Table 4.9

Correlation Analysis between Net profit & Loan & Adv.

r	r²	P.E.	6 P.E.	Remarks
0.0259	0.0007	0.2132	1.2789	Insignificant

(Source: Appendix III)

The table showed that the relationship between net profit after tax and loan and advances was positive. The correlation coefficient between these two variables was 0.0259. Similarly, the coefficient of determination was 0.0007, which indicated that 0.07% change in the net profit was explained by the change in loan and advances, which was very low. Further, the calculated probable error in the relation was 0.2132. Since, the correlation coefficient between net profit and total loan was lower than the calculated 6 P.E., [i.e. $r (0.0259) < 6 \text{ P.E.} (1.2789)$], the relationship between net profit and total loan was statistically insignificant and thus it was not necessary that net profit should increase with the increase in loan and advances and vice versa.

4.1.6.1.2 Correlation Analysis between Loan & Advances & Total Deposit

A bank needs to have good synchronization between loan and advances and total deposit to effectively mobilize the fund collected. To measure the degree of relationship between these two variables, the correlation coefficient has been determined.

Table 4.10

Correlation Analysis between Loan & Advances and Total Deposit

r	r²	P.E.	6 P.E.	Remarks
0.3515	0.1235	0.1869	1.1217	Insignificant

(Source: Appendix III)

The table showed that there was low positive relationship between loan and advances and total deposit of RBB, since the correlation coefficient between these two variables was 0.3515. Further, the coefficient of determination indicated that 12.35% variation in loan and advances was caused by change in total deposit. In addition, the calculated value of probable error and 6 P.E. were 0.1869 and 1.1217 respectively. However, the lower value of 'r' than the 6 P.E. ($r = 0.3515 < 6 \text{ P.E.} = 1.1217$) indicated that the relationship between total deposit and loan and advances was statistically insignificant. Hence, there were other variables that had positive relationship with loan and advances rather than deposit.

4.1.6.1.3 Correlation Analysis between Loan & Advances and Investment

A bank needs good investment policy and lending policy to reap greater amount of profit. Thus, to test whether these two variables are interrelated, the correlation between them has been tested.

Table 4.11

Correlation Analysis between Loan & Advances and Total Investment

r	r²	P.E.	6 P.E.	Remarks
0.1473	0.0217	0.2087	1.2520	Insignificant

(Source: Appendix III)

The above table presented the relationship between loan and advances and total investment. The correlation coefficient of 0.1473 indicated that there was low positive relationship between these two variables. Since the value of 'r' was lower than the 6 P.E. ($r = 0.1473 < 6 \text{ P.E.} = 1.2520$), the relationship between these two variables was statistically insignificant. Thus, loan and advances was not dependent on investment.

4.1.6.1.4 Correlation Analysis between Non Performing Loan and Loan & Advances

Lower the non performing loan is considered better for the bank and to have sound earning capacity. To test whether there exist any relation between non performing loan and loan and advances, the correlation coefficient has been calculated and tested through probable error.

Table 4.12

Correlation Analysis between Non Performing Loan and Loan & Advances

r	r²	P.E.	6 P.E.	Remarks
-0.1569	0.0246	0.2080	1.2483	Insignificant

(Source: Appendix III)

Similarly, the table showed that non performing loan had inverse relationship with loan and advances, and hence NPL decreases/increases with the increase/decrease of loan and advances. The correlation coefficient between these two variables was -0.1569. However, since the absolute value of 'r' was

lower than the 6 P.E. ($t = 0.1569 < 6 \text{ P.E.} = 1.2483$), the relationship between these two variables was insignificant.

4.1.6.2 Regression Analysis

The regression analysis computes by what amount the dependent variable will fluctuate on per unit changes on the independent variable. Under this analysis, the regression line of net profit on loan and advances, loan and advances on total deposit, loan and advances on total investment, and non performing assets on loan and advances have been calculated.

4.1.6.2.1 Regression Analysis of Net Profit on Loan & Advances

Let net profit of RBB be the dependent variable on loan and advances disbursed. Then the regression equation calculated by assuming this relation is presented in the table below.

Table 4.13

Regression Analysis between Net profit and Loan & Advances

a	b	Regression Equation
-1794.43	-0.02	NPAT = -1794.43 - 0.02 LA

(Source: Appendix III)

The above table shows the regression line of net profit and loan and advances. The table depicts that the net profit has negative relationship with the total loan, which clearly indicates the poor management of RBB in loan, and thus there is uncertainty in interest amount from the loan disbursed and hence greater chances of default loan, which ultimately deduct the net profit of the bank. The regression line shows that if other thing, -1794.43, remains constant, the net profit of the bank decreases by Rs. 0.02 with per rupee increment in loan and advances.

4.1.6.2.2 Regression Analysis of Loan and Advances on Total Deposit

Considering loan and advances as the dependent variable on total deposit, the regression equation calculated between these two variables is presented in the table below.

Table 4.14

Regression Analysis between Loan & Advances on Total Deposit

a	b	Regression Equation
21570.69	0.14	$LA = 21570.69 + 0.14 TD$

(Source: Appendix III)

The regression line of loan and advances on total deposit indicates that with per rupee increment in total deposit, the loan and advances of RBB increases by Rs. 0.14. Thus, loan and advances has positive relationship with the total deposit collection of the bank. Further, it can be said that loan and advances is one of the major uses of total deposit of RBB.

4.1.6.2.3 Regression Analysis of Loan and advances on Investment

Let the disbursement of loan and advances depends upon the investment policy of the bank. Then the regression equation of loan and advances on total investment of RBB is presented below;

Table 4.15

Regression Analysis between Loan & Advances on Total Investment

a	b	Regression Equation
26861.01	0.13	$LA = 26861.01 + 0.13 TI$

(Source: Appendix III)

The above table presented the relationship between loan and advances and total investment. The regression line clarified that with per rupee increment in total investment led to Rs. 0.13 increase in loan and advances, if the other variable, Rs. 26861.01, remains constant.

4.1.6.2.4 Regression Analysis of NPL on Loan & Advances

Assuming non performing loan is dependent on the loan and advances disbursed, the regression line of non performing loan on loan and advances has been calculated, which is presented in the below table;

Table 4.16

Regression Analysis between Non Performing Loan and Loan & Advances

a	b	Regression Equation
15423.75	-0.15	$NPL = 15423.75 - 0.15 LA$

(Source: Appendix III)

Similarly, the table showed that non performing loan had negative relationship with loan and advances, and hence NPL decreases/increases with the increase/decrease of loan and advances. The regression line indicated that with per rupee increase in loan and advances, the NPL decreases by Rs. 0.15, if the variable, 15423.75, remains stable.

4.1.6.3 Trend Analysis

To estimate the value of loan and advances, deposit, investment, non performing loan and net profit in the forthcoming four fiscal years, i.e. in the fiscal year 2009/10, 2010/11, 2011/12, and 2012/13, the trend analysis has been done. The loan and advances, deposit, investment, non performing loan and net profit have been considered dependent variables on the time. Then the regression line and predicted value calculated have been shown in the below tables.

4.1.6.3.1 Trend Analysis of Loan and Advances

To estimate the value of loan and advances in the next four fiscal year periods, the loan and advances has been considered as the dependent variable (Y) on the time period (X), independent variable. Then the trend value calculated using the trend analysis has been presented in table below.

Table 4.17

Trend Analysis of Loan and Advances

FY	Actual	Trend
1999/00	34744.27	28127.21
2000/01	27375.13	28089.12
2001/02	27037.37	28051.02
2002/03	26608.83	28012.93
2003/04	25105.68	27974.84
2004/05	27000.93	27936.75
2005/06	23246.51	27898.65
2006/07	24871.36	27860.56
2007/08	27524.92	27822.47
2008/09	36042.93	27784.38
2009/10		27746.28
2010/11		27708.19
2011/12		27670.10
2012/13		27632.01
Trend Line	$Y_{LA} = 28165.30 - 38.09 X_{Yr}$	

(Source: Appendix – IV)

The above table has estimated the value of loan and advances for the next four fiscal years. The table depicts that the loan and advances for the fiscal year 2009/10, 2010/11, 2011/12 and 2012/13 will be Rs. 27746.28 millions, Rs. 27708.19 millions, Rs. 27670.10 millions and rs. 27632.01 millions respectively. Similarly, the trend line of loan advances on time period indicates that in each year, the loan and advances of RBB decreases by Rs. 38.09 millions, if the other variable, 28165.30, remains constant. Hence, loan and advances has negative relationship with time period.

4.1.6.3.2 Trend Analysis of Total Deposit

Let Y be the total deposit, dependent variable, and X be the time period, independent variable. Then the trend value of total deposit, using such relation, is presented in the table below.

Table 4.18
Trend Analysis of Total Deposit

FY	Actual	Trend
----	--------	-------

1999/00	38575.14	33148.55
2000/01	40773.66	36242.73
2001/02	38993.29	39336.90
2002/03	39402.27	42431.08
2003/04	40866.77	45525.26
2004/05	43016.06	48619.43
2005/06	46195.48	51713.61
2006/07	50464.13	54807.79
2007/08	64340.95	57901.96
2008/09	68095.70	60996.14
2009/10		64090.32
2010/11		67184.49
2011/12		70278.67
2012/13		73372.85
Trend Line	$Y_{TD} = 30054.37 + 3094.18 X_{Yr}$	

(Source: Appendix – IV)

The above table clarifies that total deposit of RBB has positive relationship with the time period, which is a good indication for RBB. The total deposit of RBB increases by Rs. 3094.18 millions per year, if the variable, 30054.37, remains uniform. The estimated value of total deposit of RBB will be Rs. 64090.32 millions, Rs. 67184.49 millions, Rs. 70278.67 millions and Rs. 73372.85 millions in the fiscal year 2009/10, 2010/11, 2011/12 and 2012/13 respectively.

4.1.6.3.3 Trend Analysis of Total Investment

To calculate the trend value of total investment, the investment has been considered as the dependent variable on time period, independent variable. The calculated trend value of total investment has been presented below.

Table 4.19
Trend Analysis of Total Investment

FY	Actual	Trend
1999/00	4336.75	2134.95
2000/01	5646.44	3540.31
2001/02	4159.47	4945.67

2002/03	4623.13	6351.03
2003/04	3117.02	7756.39
2004/05	8415.88	9161.75
2005/06	11555.36	10567.11
2006/07	12650.20	11972.47
2007/08	14443.38	13377.83
2008/09	15643.05	14783.19
2009/10		16188.55
2010/11		17593.91
2011/12		18999.27
2012/13		20404.63
Trend Line	$Y_{TI} = 729.59 + 1405.36 X_{Yr}$	

(Source: Appendix – IV)

Alike total deposit, the investment of RBB will also increase in the forthcoming years. The investment of RBB will increase by Rs. 1405.36 millions per year, if the variable 729.59 remains constant. Thus, investment will have direct relationship with total deposit. The trend value of investment for the fiscal year 2009/10 will be Rs. 16188.55 millions, the fiscal year 2010/11 will be Rs. 17593.91 millions, the fiscal year 2011/12 Rs. 18999.27 millions, and the fiscal year 2012/13 will be Rs. 20404.63 millions.

4.1.6.3.4 Trend Analysis of Non Performing Loan

Lower the non performing loan reflects better loan management in the bank. Thus, to forecast whether the non performing loan will decrease in the four forthcoming years, the non performing loan has been considered as dependent variable on time.

Table 4.20
Trend Analysis of Non Performing Loan

FY	Actual	Trend
1999/00	13661.45	16072.48
2000/01	12209.31	14995.79
2001/02	14889.48	13919.10
2002/03	16005.21	12842.41
2003/04	14470.91	11765.72
2004/05	13689.47	10689.04

2005/06	8622.13	9612.35
2006/07	7120.67	8535.66
2007/08	5953.64	7458.97
2008/09	5651.53	6382.28
2009/10		5305.59
2010/11		4228.90
2011/12		3152.21
2012/13		2075.52
Trend Line	$Y_{NPL} = 17149.17 - 1076.69 X_{Yr}$	

(Source: Appendix – IV)

Similarly, alike loan and advances, the non performing loan of RBB will also decrease in the forthcoming years. The non performing loan of RBB decreases by Rs. 1076.69 millions per year, if the other variable remains stable. The table shows that the forecasted value of non performing loan will be Rs. 5305.59 millions in the fiscal year 2009/10, Rs. 4228.90 millions in the fiscal year 2010/11, Rs. 3152.21 millions in the fiscal year 2011/12, and Rs. 2075.52 millions in the fiscal year 2012/13.

4.1.6.3.5 Trend Analysis of Net Profit after Tax

Higher the net profit is favorable for any institution. So, to forecast whether, the net profit of RBB will increase in the forthcoming four years, the net profit has been considered as the dependent variable on time period. The calculated trend value of net profit is presented in the table below.

Table 4.21
Trend Analysis of Net Profit after Tax

FY	Actual	Trend
1999/00	-1791.46	-5490.83
2000/01	-7083.25	-4522.39
2001/02	-7068.25	-3553.95
2002/03	-4839.78	-2585.50
2003/04	1040.10	-1617.06
2004/05	1322.89	-648.62
2005/06	1591.49	319.83
2006/07	1697.09	1288.27
2007/08	1770.55	2256.71

2008/09	2032.23	3225.15
2009/10		4193.60
2010/11		5162.04
2011/12		6130.48
2012/13		7098.93
Trend Line	$Y_{NPAT} = -6459.28 + 968.44 X_{Yr}$	

(Source: Appendix – IV)

Further, the net profit of RBB will have positive relationship with the time period, which means that net profit increases in each fiscal year by Rs. 968.44 millions, if the variable -6459.28 remains rigid. Consequently, the estimated value of net profit in the fiscal year 2009/10 will be Rs. 4193.60 millions, in the fiscal year 2010/11 will be Rs. 5162.04 millions, in the fiscal year 2011/12 will be Rs. 6130.48 millions, and in the fiscal year 2012/13 will be Rs. 7098.93 millions.

4.2 Primary Data Analysis

To examine the loan management situation, the primary data has also been undertaken. For the primary data collection, mainly the questionnaire containing 10 questions has been performed. The 30 respondents: 10 investors, 10 employees of banks, and 10 borrowers, have been chosen for the questionnaire purpose. The Investors are chosen randomly from the NEPSE floor, whereas the banks employees and Borrower are chosen by visiting the sampled banks.

4.2.1 Loan Management Efficiency

Granting loan is the major function of the bank and loan is considered as the major source of interest income. Thus, efficiency in managing loan is crux for the survival of bank. To know whether the RBB is efficient in loan management, the respondents were asked on this matter.

Table 4.22

Efficiency in Loan Management

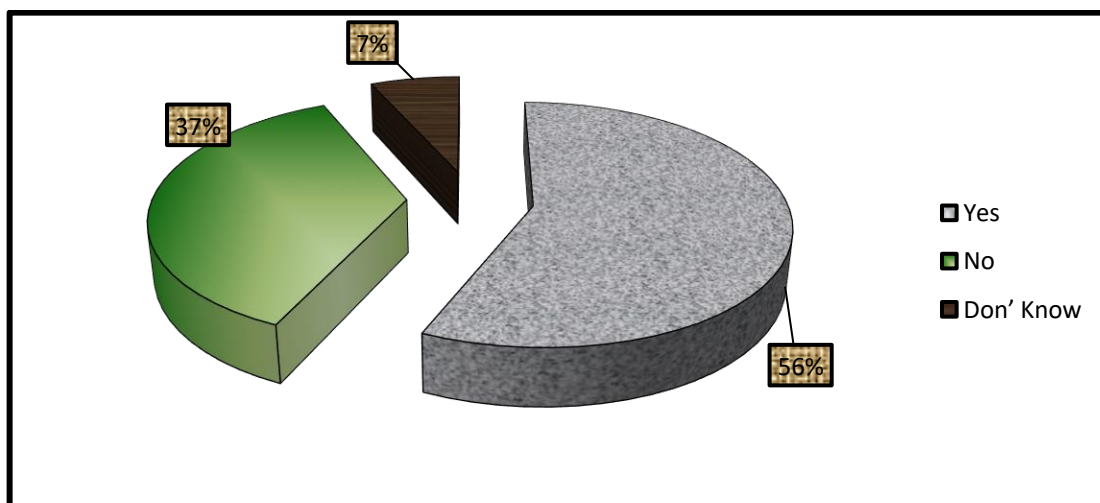
Answer	Investor	Employee	Borrower	Total
---------------	-----------------	-----------------	-----------------	--------------

	No.	%	No.	%	No.	%	No.	%
Yes	6	60	7	70	4	40	17	56
No	4	40	2	20	5	50	11	37
Don' Know	0	0	1	10	1	10	2	7
Total	10	100	10	100	10	100	30	100

(Source: Field Survey, 2010)

The table reveals that the majority of the respondents, i.e. 56% (17 out of 30), has opined that the commercial banks are efficient in loan management, while 37% of the respondents has said that the banks are not efficient in managing loan and 7% remained has said don't know. Looking each category, the majority of the Investors, i.e. 60% (6 out of 10), and bank employee, i.e. 70% (7 out of 10), has stated that the banks are efficient in managing credit, while the majority of borrower, 50% (5 out of 10), has opined that the banks are not efficient in managing credit. Hence, overlooking the overall majority, it can be concluded that the RBB is efficient in managing credit. However, it will be better, if the bank traces out the dissatisfaction of borrower in the management of loan by bank.

Figure 4.9
Efficiency in Loan Management



4.2.2 Loan Floatation Basis

To examine the most important basis that should be considered while disbursing loan, the respondents have been asked to express their view. The responses obtained from them have been presented in the table 4.23.

Table 4.23

Loan Floatation Basis

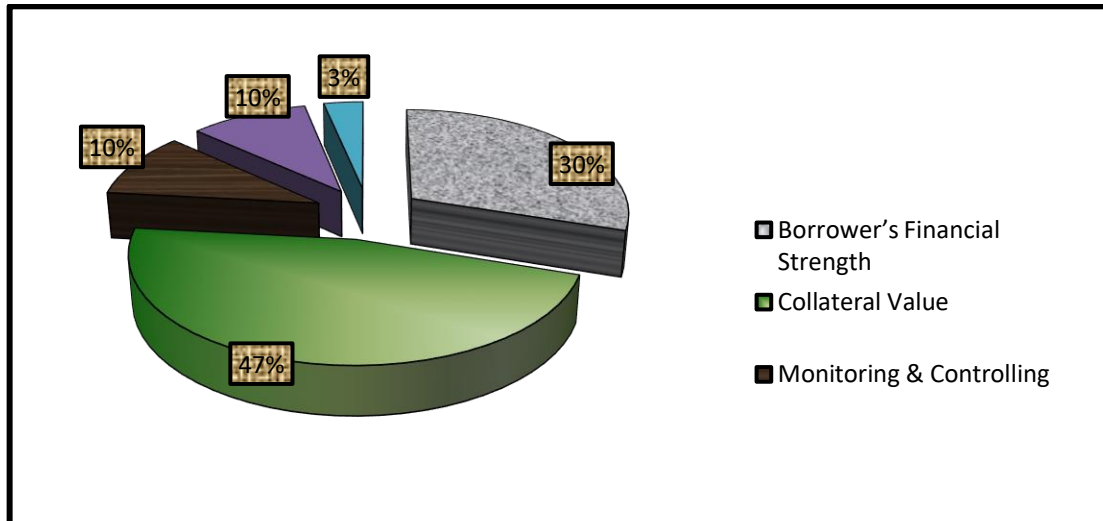
Basis	Investor		Employee		Borrower		Total	
	No.	%	No.	%	No.	%	No.	%
Borrower's Financial Strength	2	20	4	40	3	30	9	30
Collateral Value	4	40	5	50	5	50	14	47
Monitoring & Controlling	2	20	0	0	1	10	3	10
Nature of Guarantor	1	10	1	10	1	10	3	10
Portfolio Management	1	10	0	0	0	0	1	3
Total	10	100	10	100	10	100	30	100

(Source: Opinion Survey, 2010)

The Table shows that the majority of the respondents have stated that the collateral value should be given more consideration while disbursing loan. Out of the 30 respondents, 14 respondents (47%), have supported this option. Besides collateral value, 30% of the respondents, 9 out of 30, have opined that evaluation borrower's financial strength should be the main basis while floating loan. Similarly, 10% of the respondents (3 out of 30), 10% of the respondents (3 out of 30) and 3% of the respondents (1 out of 30) have affirmed that nature of guarantor, monitoring and controlling and portfolio of loan management respectively should be the main basis for loan floatation.

Figure 4.10

Loan Floatation Basis



4.2.3 Harassment in Paper Document

Before granting loan, the bank has to arrange various documents to ensure the payment back of principal and interest amount of loan granted. So to know whether the paper document maintain is harassing, the respondents are asked on this regard. The responses obtained from them are presented in the table below.

Table 4.24

Harassment in Paper Document

Answer	Investor		Employee		Borrower		Total	
	No.	%	No.	%	No.	%	No.	%
Yes	3	30	2	20	7	70	12	40
No	5	50	6	60	2	20	13	43
Don' Know	2	20	2	20	1	10	5	17
Total	10	100	10	100	10	100	30	100

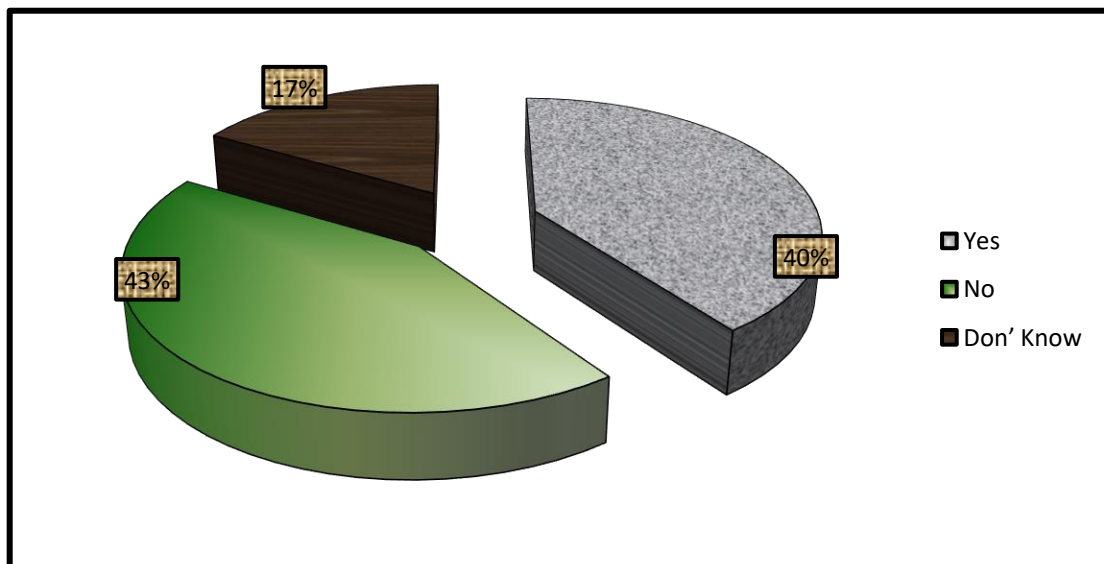
(Source: Field Survey, 2010)

The table shows that the majority of the respondents, 43% (13 out of 30), has stated that there is no harassment in paper document maintained by bank while granting loan, while 40% of the respondents (12 out of 30) has affirmed that the paper documentation is harassing and 17% of the respondents (5 out of 30) has remained neutral. Gazing each category, the majority of Investors, i.e. 50%

(5 out of 10), and bank's employees, 60% (6 out of 10), have said that the paper documentation is not harassing, while the majority of the Borrower, 70% (7 out of 10), has said that the paper documentation is harassing. Considering the overall responses, it can be concluded that the paper documentation maintained by commercial banks before granting loan is not harassing. However, the banks should not ignore the oppose opinion of Borrower and should make the paper documentation comfortable.

Figure 4.11

Harassment in Paper Document



4.2.4 Satisfaction in Mortgage Value

To ensure the payment of loan by the Borrower, the bank keeps mortgage after the valuing it. So to know whether the valuation done by bank is satisfactory, the respondents are asked on this matter. The respondents obtained from them are presented in the table below.

Table 4.25

Satisfaction in Mortgage Value

Answer	Investor		Employee		Borrower		Total	
	No.	%	No.	%	No.	%	No.	%
Yes	4	40	6	60	8	80	18	60

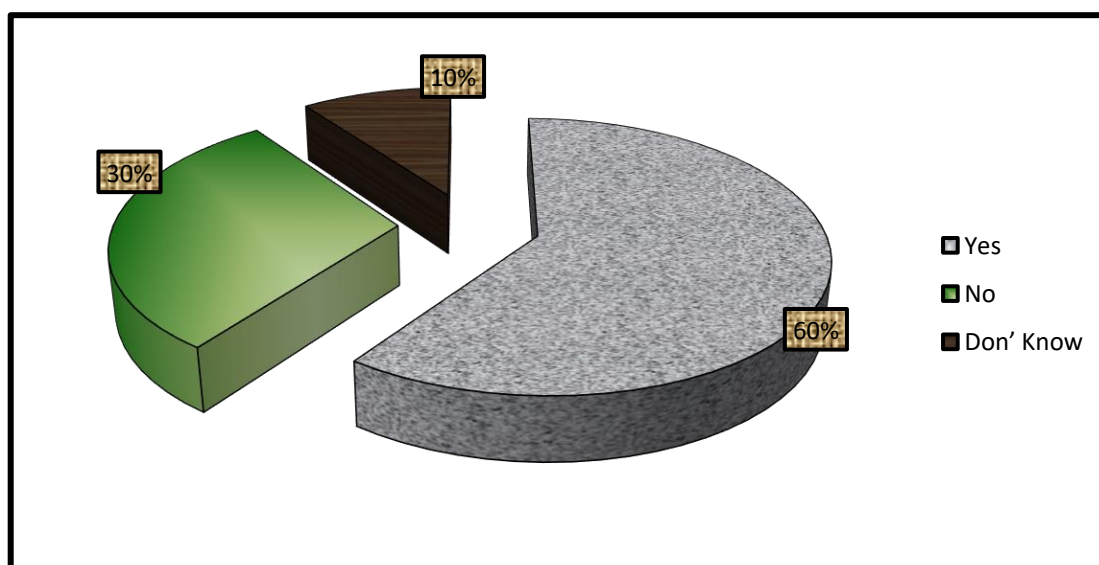
No	4	40	3	30	2	20	9	30
Don' Know	2	20	1	10	0	0	3	10
Total	10	100	10	100	10	100	30	100

(Source: Field Survey, 2010)

The table reveals that 40%, 40% and 20% of the Investor states that the mortgage valuation done by commercial banks is satisfactory, not satisfactory and don't know respectively. Similarly, 60% of the bank employees say that the valuation is satisfactory, 30% has said the valuation is not satisfactory and 10% has remained neutral. Likewise, 80% and 20% of the borrower has said that the valuation is satisfactory and not satisfactory respectively. In overall, 60% of the total respondents have state that the valuation is satisfactory, while 30% stated that the valuation is not satisfactory and 10% remained neutral. Considering the overall majority, it can be concluded that the valuation of mortgage value done by bank before disbursing loan is satisfactory.

Figure 4.12

Satisfaction in Mortgage Value



4.2.5 Involvement in Valuation

To examine from whom the valuation of mortgage should be done before granting loan, the respondents are asked on this matter. The responses obtained from each category and in total have been presented in the table below.

Table 4.26

Involvement in Valuation

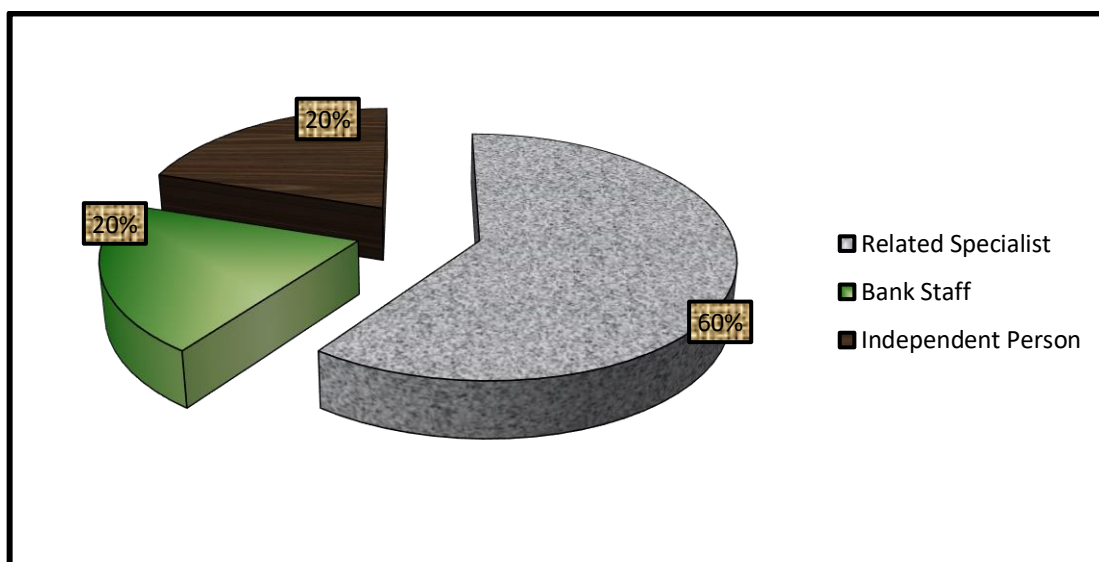
Answer	Investor		Employee		Borrower		Total	
	No.	%	No.	%	No.	%	No.	%
Related Specialist	8	80	4	40	6	60	18	60
Bank Staff	0	0	6	60	0	0	6	20
Independent Person	2	20	0	0	4	40	6	20
Total	10	100	10	100	10	100	30	100

(Source: Field Survey, 2010)

The above table depicts that the majority of the Investors, 80%, has stated that the valuation should be done by the related specialist, while 20% of the Investors has said that the valuation should be done by the independent person appointed by the mutual agreement between bank and borrower. Similarly, 60% of the bank employee has stated that the valuation should be done by the bank staff and 40% has said that the valuation should be done by related specialist. Likewise, 60% and 40% of the borrower has opined that the mortgage valuation should be done by related specialist and the independent person respectively.

In overall, 60% (18 out of 30), 20% (6 out of 30) and 20% (6 out of 30) of the respondents has said that the mortgage valuation should be done by related specialist, bank staff and independent person respectively. Considering the overall majority, it can be concluded that the valuation of mortgage would be satisfactory, if it has been done by related specialist.

Figure 4.13
Involvement in Valuation



4.2.6 Time to Disburse Loan

The bank takes certain time for loan approval after it receives the application form. Thus, to know how many days will be the best time to disburse credit, the respondents are asked on this matter. The responses obtained from them are presented in the table below.

Table 4.27
Time to Disburse Loan

Answer	Investor		Employee		Borrower		Total	
	No.	%	No.	%	No.	%	No.	%
5-10 days	3	30	2	20	4	40	9	30
10-20 days	6	60	7	70	6	60	19	63
Above 20 days	1	10	1	10	0	0	2	7
Total	10	100	10	100	10	100	30	100

(Source: Field Survey, 2010)

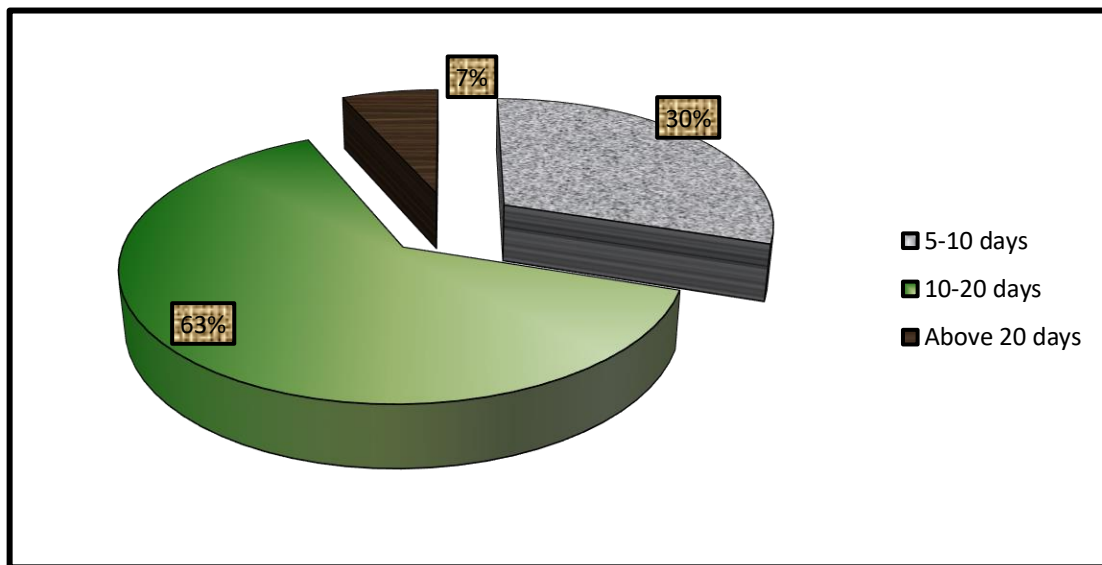
The above table reveals that the majority of the Investors, i.e. 60%, has stated that 10-20 days after the application received by the bank would be the appropriate time to disburse loan, while 30% and 10% of the Investors has opined 5-10 days and above 20 days as the appropriate time. Similarly, 20%, 70% and 10% of the bank employees has indicated 5-10 days, 10-20 days and above 20 days as the appropriate time to disburse loan after the receipt of

application. Likewise, 40% and 60% of the Borrower has opined 5-10 days and 10-20 days as the appropriate time to disburse loan.

In overall, 30%, 63% and 7% of the total respondents has opined 5-10 days, 10-20 days and above 20 days respectively to be the appropriate time to disburse loan after the receipt of application. Hence, considering the overall majority of each group and overall, it can be concluded that 10-20 days would be the best time to disburse loan after receiving the application.

Figure 4.14

Time to Disburse Loan



4.2.7 Degree of Effect of NPA on Banking Industry

To know the degree of effect that NPA has on banking industry, the respondents are asked to express their view. The responses obtained from them have been presented in the Table 4.28.

Table 4.28

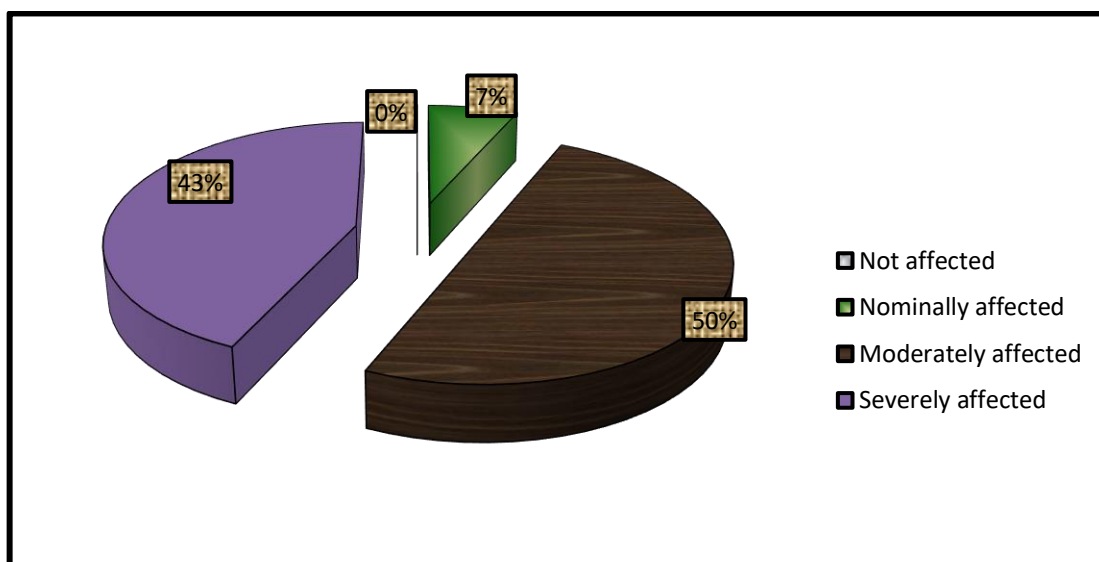
Degree of Effect of NPA on Banking Industry

Basis	Investor		Employee		Borrower		Total	
	No.	%	No.	%	No.	%	No.	%
Not affected	0	0	0	0	0	0	0	0
Nominally affected	0	0	1	10	1	10	2	7
Moderately affected	6	60	6	60	3	30	15	50
Severely affected	4	40	3	30	6	60	13	43
Total	10	100	10	100	10	100	30	100

(Source: Opinion Survey, 2010)

The table 4.28 demonstrates that 50% of the respondents, 15 out of 30, have stated that the banking industry has been moderately affected by the problem of NPA. Similarly, 43% of the respondents, 13 out of 30, have said that the problem of NPA has severe effect on the banking industry. Also, 7% of the respondents, 2 out of 30, have stated that the banking industry had been nominally affected by the problem of NPA. Looking each category, the majority of the investors, 6 out of 10 and the majority of the employees, 6 out of 10, have stated that banking industry has been moderately affected by NPA. However, the majority of the borrower, 6 out of 10, stated that the banking industry has been severely affected by the problem of NPA. Finally, considering the overall majority, 15 out of 30, it can be concluded that NPA has moderate effect on banking industry.

Figure 4.15
Degree of Effect of NPA on Banking Industry



4.2.8 Best Time to Follow up after Due date

To examine the best time within which the bank should follow up for recovery after due date, the respondents have been asked on this regard. The responses obtained from them have been presented in the Table 4.29.

Table 4.29

Best Time to Follow up after Due date

Basis	Investor		Employee		Borrower		Total	
	No.	%	No.	%	No.	%	No.	%
Within a week	2	20	3	30	1	10	6	20
Within two weeks	5	50	6	60	2	20	13	43
Within a month	3	30	1	10	5	50	9	30
After one month onwards	0	0	0	0	2	20	2	7
Total	10	100	10	100	10	100	30	100

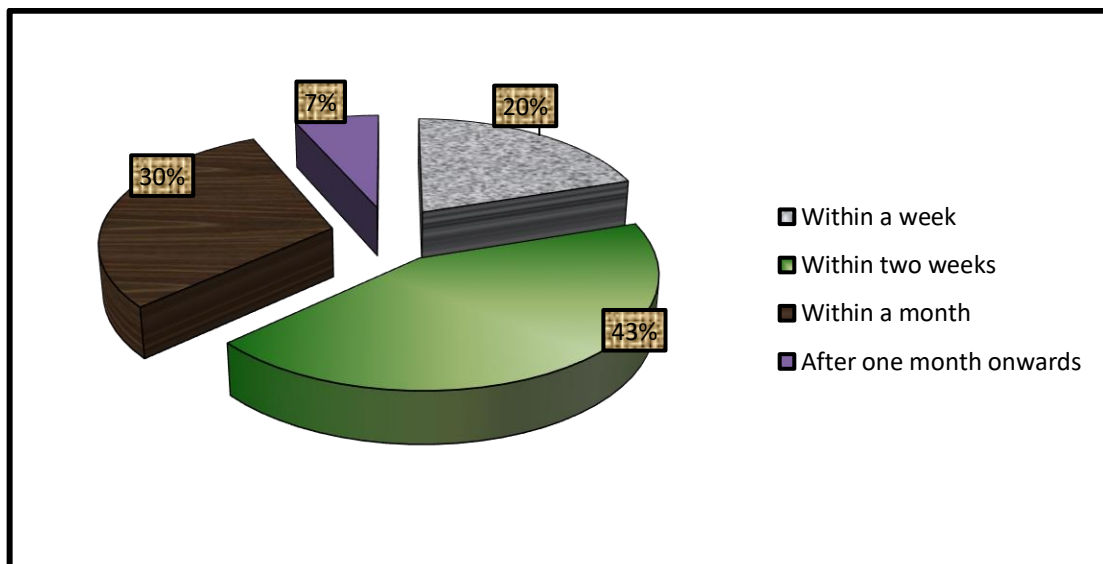
(Source: Opinion Survey, 2010)

The table demonstrates that 43% of the respondents, 13 out of 30, are in the view that banks should follow up for the recovery within two weeks after due date. Similarly, 30% of the respondents, 9 out of 30, have opined that within a month after due date will be the best time that the bank should start for recovery. Also, 20% of the respondents, 6 out of 30 and 7% of the respondents, 2 out of 30, opined that within a week and after one month onward respectively

will be the best time for follow up. Looking each category, the majority of investors, 5 out of 10 and the majority of employees, 6 out of 10, have supported within two weeks, whereas the majority of borrowers, 5 out of 10, have supported within a month for follow up after due date. Eventually, considering the overall majority, it can be concluded that within two weeks after the matured date of loan will be the best time for bank to follow up for recovery process.

Figure 4.16

Best Time to Follow up after Due date



4.2.9 Most Influencing Factor in Loan disbursement

To investigate what factor is the most influencing in granting credit, the respondents are asked on this matter. The responses obtained from them are summarized in the table in the rank form.

Table 4.30

Most Influencing Factor in Loan disbursement

Influencer	Basis	Rank					Total	Weight	Mean Wt.	Overall Rank
		1	2	3	4	5				
Paper Document	Investor	1	0	2	3	4	10	39	3.90	5
	Employee	1	2	1	3	3	10	35	3.50	4
	Borrower	0	1	2	4	3	10	39	3.90	4
	Total	2	3	5	10	10	30	113	3.77	4
Time Period	Investor	1	1	0	5	3	10	38	3.80	4
	Employee	2	2	2	1	3	10	31	3.10	3
	Borrower	0	1	4	3	2	10	36	3.60	3
	Total	3	4	6	9	8	30	105	3.50	3
Employee Behavior	Investor	0	2	3	2	3	10	36	3.60	3
	Employee	1	0	3	2	4	10	38	3.80	5
	Borrower	1	0	2	2	5	10	40	4.00	5
	Total	2	2	8	6	12	30	114	3.80	5
Interest Rate	Investor	5	3	2	0	0	10	17	1.70	1
	Employee	4	2	2	2	0	10	22	2.20	1
	Borrower	5	5	0	0	0	10	15	1.50	1
	Total	14	10	4	2	0	30	54	1.80	1
Collateral Value	Investor	3	4	3	0	0	10	20	2.00	2
	Employee	2	4	2	2	0	10	24	2.40	2
	Borrower	4	3	2	1	0	10	20	2.00	2
	Total	9	11	7	3	0	30	64	2.13	2

(Source: Field Survey, 2010)

The above table shows that the interest rate charged on the loan amount is the most influencing factor while granting loans. The respondents have ranked 1 for interest rate chargeable, 2 for the collateral value, 3 for time period taken for granting credit, 4 for paper documentation required, and 5 for the behavior of bank's employee to the customer. In overall, the majority of the respondents, 14 out of 30, have opined that the interest rate is the most influencing factor in loan disbursement. Thus, it will be worthwhile if bank charges the appropriate interest rate for effective Loan management.

4.2.10 Suggestions for Effective Loan Management

At the end of the questionnaire, the respondents are asked to give their valuable suggestion for the effective Loan management. The responses obtained from them, in the rank form, have been presented in the table below.

Table 4.31
Suggestions for Effective Loan Management

Remedy	Basis	Rank				Total	Weight	Mean Wt.	Overall Rank
		1	2	3	4				
Careful Evaluation	Investor	4	3	3	0	10	19	1.90	1
	Employee	3	5	2	0	10	19	1.90	1
	Borrower	5	5	0	0	10	15	1.50	1
	Total	12	13	5	0	30	53	1.77	1
Appropriate Interest	Investor	3	4	3	0	10	20	2.00	2
	Employee	3	4	3	0	10	20	2.00	2
	Borrower	4	4	2	0	10	18	1.80	2
	Total	10	12	8	0	30	58	1.93	2
Consumer Awareness	Investor	0	1	3	6	10	35	3.50	4
	Employee	0	0	3	7	10	37	3.70	4
	Borrower	0	0	3	7	10	37	3.70	4
	Total	0	1	9	20	30	109	3.63	4
Timely Collection	Investor	3	2	1	4	10	26	2.60	3
	Employee	4	1	2	3	10	24	2.40	3
	Borrower	1	1	5	3	10	30	3.00	3
	Total	8	4	8	10	30	80	2.67	3

(Source: Field Survey, 2010)

The above table depicts that the respondents ranked 1 for careful evaluation of loan proposal, 2 for appropriate interest rate to be charged, 3 for collection of loan at regular time interval and 4 for consumer awareness, as the suggestion for effective Loan management of the bank. Out of 30 respondents, 12 ranked 1 for careful evaluation. So, it can be concluded that the bank can have sound management of credit, if it evaluates the Loan proposal carefully. Also, the bank interest rate should not be high, as a result the Borrower feel burden while paying interest amount.

4.3 Major Findings of the Study

After careful analysis of both the secondary and primary data available, the following major findings have been drawn;

Findings from Secondary Data Analysis

- a. Since the loan investment per year represented only 12.79% of the total loan outstanding in average, it can be said that RBB necessitates strong recovery policy to decrease the outstanding amount.
- b. The average collection for the ten year was 6.04% of the total loan outstanding. It also indicates that RBB needs strong recovery policy.
- c. The loan investment grew by 150.88% in the previous five year period, by 101.85% in the last five year period and by 126.36% in ten year period. Similarly, the loan outstanding decreased by 1.58% in the previous five year period, grew by 8.45% in the current five year period and grew by 3.44% in the ten year period. Likewise, the loan recovery by 11.36%, 1.87%, and 6.61% in the previous five year period, current five year period and the whole ten year period in average.
- d. The non performing loan covered 41.05% of the total loan in average. This coverage indicated that the loan on RBB was much risky. Further, RBB made 36.68% of the total loan as loan loss provision in average.
- e. Almost two third of the deposit had been mobilized in granting loan and advances. The deposit mobilization rate of RBB on loan was 61.83% in average.
- f. The statistical analysis revealed that there existed insignificant relationship between net profit and loan and advances, between loan and advances and total deposit, between loan and advances and total investment, and between non performing loan and loan and advances.
- g. The trend value indicated that loan and advances decreases by Rs. 38.09 millions, total deposit increases by Rs. 3094.18 millions, total investment increases by Rs. 1405.36 millions, non performing loan decreases by Rs. 1076.69 millions, and net profit increases by Rs. 968.44 millions in each forthcoming fiscal year.

Findings from Primary Data Analysis

- a. 56% of the respondents agreed that the RBB is efficient in loan management. Also, 43% of the respondents have said that there is no harassment in the paper document requirement by bank while disbursing loan.
- b. 47% of the respondents are in the view that the collateral evaluation should be the main basis to be considered while disbursing loan.
- c. Further the majority of the respondents, 60%, are satisfied in the mortgage valuation done by bank. Also, same percentage, 60%, has stated that related specialist should be involved in mortgage valuation rather than bank staff and independent person.
- d. The majority of the respondents, 63%, have opined that 10-20 days will be the appropriate time to disburse loan after the bank receives application.
- e. Similarly, 50% of the respondents, 15 out of 30, have stated that the banking industry has been moderately affected by the problem of NPA. And 41% of the respondents suggested within two weeks after the due date will be the best time to follow up for loan recovery
- f. In ranking the most influencing factor in loan disbursement, interest rate chargeable got rank 1, while collateral value got rank 2. Thus, interest rate of the bank is the most influencing determinants of loan. Eventually, the respondents have suggested that careful evaluation of the loan proposal before granting loan.

CHAPTER – V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

The prosperity of banking system depends on the two major functions, viz, deposit collection and lending. At present situation, deposit collection is not much difficult, as liquidity of overall banking system is rising up. But the lending function is not like that, as banks are facing two major challenges in lending. First of all, due to unfavorable political environment and violence, businessmen are reluctant to invest in business, so the volume of loan and advances is not in regular trend and if loan is given, the problem of turning loan to non-performing is another challenge that banks are facing. In addition, various risk like credit risk, interest rate risk, liquidity risk, price risk, foreign exchange risk, transaction risk and so on are associated with lending. So, to disburse loan in the most productive and secure sector has become the target of each bank. Thus, effective management of the loan and the credit function is fundamental to a bank's safety and soundness.

Loan management (LM) is the process by which risks that are inherent in the credit process are managed and controlled. Because review of the LM process is so important, it is a primary supervisory activity. Assessing LM involves evaluating the steps bank management takes to identify and control risk throughout the credit process. The assessment focuses on what management does to identify issues before they become problems. Each bank pays special concentration on managing loan, since loan is the main source of interest income. Rastriya Banijya Bank is also on the same runway and provides loan with the hope of increasing its net profit by collecting maximum amount of interest.

The study has been conducted with the objective of giving true insight of loan management in RBB. To achieve the objectives of the study, different financial

and statistical tools have been adopted. All of the analysis made revolves within the secondary data that have been collected mainly through the account department of concerned bank and primary data collected from the investors, employees and borrowers of the bank.

For the convenience, the study has been divided mainly into five main chapter, viz, a) Introduction, b) Review of Literature, c) Research Methodology, d) Data Presentation and Analysis and e) Summary, Conclusion and Recommendations.

5.2 Conclusion

On the basis of secondary data analysis and the major findings drawn in the fourth chapter, it can be concluded that RBB lacks appropriate loan investment policy, since the loan investment represented only the small percentage of the loan outstanding. Also, the loan recovery policy of RBB has been aggravated during the periods. Thus, an efficient loan policy is crux for the enhancement of the performance of the bank. Further, the inconsistency in the growth rate of loan outstanding, loan investment and loan recovery also sought a sound loan management policy in bank. Although the chance of turning loan into default is lower in the recent periods than in previous, RBB should make effort to prevent the loan from becoming loss loan. In addition, it can be concluded that almost three-fifth of the deposit have been invested in granting loan and advances to earn interest income. Thus, loan and advances was the major use of deposit in RBB.

The statistical analysis aid to conclude that RBB lacks strong synchronization between loan & advances and net profit, loan & advances and non performing loan, loan & advances and total deposit, and loan & advances and total investment, since the relationship between them was statistically insignificant. However, on the basis of trend analysis, it can be considered that the loan and advances in the forthcoming year will decrease, the collection of deposit amount will increase, the total investment amount will increase, the non

performing loan will decrease and the net profit will increase. Hence, a good financial performance of the bank can be expected in the future.

Eventually, on the basis of primary data analysis, it can be concluded the bank is efficient in managing loan, and the process of getting loan from RBB is not difficult and thus there is no paper harassment. Further, it can be stated that collateral evaluation should be the main basis to be considered while disbursing loan. Also, it can be assumed that one will be satisfied in the mortgage valuation done by bank. In addition, the bank has not been extremely affected by the problem of NPA and to decrease the credit risk, the bank should follow up the recovery policy just within two weeks after the due date. Finally, interest rate is the most influencing factor in loan disbursement in RBB and careful evaluation of the loan proposal is crux for the bank.

5.3 Recommendations

On the basis of major findings drawn in the fourth chapter and the conclusion drawn in this chapter, the following recommendations have been provided for the enhancement of loan management of RBB;

- Short term loan must be largely distributed. This will help to utilize small and local resources.
- Actual loan investment and collection is always lower than the targeted investment. Therefore, the bank should maintain the investment and collection according to the target, so if necessary, it should restructure in loan investment, outstanding and collection as well as all aspect of these three purposes.
- Loan investment is largely effected by recovery status. So, management should always adopt such a policy that lure the customers to pay loan before due date. Liberal action and subsidy can be schemed for this. Similarly, the outstanding loan must be in a decreasing trend.
- Supervision and inspection related to loan must be unbiased, strict and efficient.

- The banks should always seek out answers to two questions. First, how could bank make “normal” loans insuring that they are making “good” loans? Second, how could it get its money back on loans that have turned bad? Clearly, weaknesses at either stage could explain both past loan failures and present reluctance to lend.
- Non-performing loan of RBB must be at least on marginal level. Similarly, RBB must segregate more proportion of loan to its commercial banking sector by dropping unnecessary program and project.
- One method that more banks might usefully adopt is systematic review of loan losses and the incorporation of lessons learned into the training of new loan officers. RBB should consider this fact to improve its productivity.
- The heavy reliance on collateral imposes high costs on borrowers and lenders. Therefore, for collateral to work properly, RBB must be able to perfect the collateral and to dispose of quickly.
- Reputation can be effective in ensuring that borrowers fulfill their contracts. However, there is a general lack of credit reporting institutions to share information about credit-worthiness. Therefore, RBB should try to get information regarding borrower’s reputation from various sources like family, friends and others who are in touch of borrowers.
- Poor recovery is the result of weak supervision, high interest and other charges laid by the bank, political interference and poor liquidity of the borrowers. So, it is recommended that the recovery policy and procedure must be exercised strictly. Strict supervision must be made for issuing the memorandum letter; supervisor must visit at the lending field whether the borrowers utilize the total loan amount for concerned purpose or not. Supervisor must motivate the borrower to utilize the full amount of loan on particular purpose. Political interference and pressure

must be neglected. And the commitment and service charge must be reduced.

- In case of borrowers, who are able but do not repay their due loans, the bank should examine the borrowers past repayment record and corrective action must be taken immediately. In the case of borrowers, who are really unable to repay their loans, repayment schedule must be rearranged after scrutinizing the exact cause of inability.
- RBB is government-owned banks. As a result, the credibility of this bank on the comparison of private banks is more on customers. It would be better if the bank recognizes this strength and perform effectively to have better prospect in the future.
- Fraud against banks is common, but typically it should not be ignored and should try to punish; prosecutors were apparently not interested in such cases. Therefore, Bankers and prosecutors must make the prosecution of bank fraud a priority.

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