CHAPTER ONE
INTRODUCTION

1.1 Background of the Study

A cooperative organization is that business organization which is established by the economically poor people with a view to working in an organized way for their common economic upliftment. In other words, cooperative organization is an organization established by the economically poor people for freeing themselves from the exploitation of the rich. It is a voluntary association based on the principle of self-help through mutual help. It has to satisfy two objectives i.e. service as well as profit.

Cooperative refers to work together for common benefit. A Cooperative is an autonomous association of people united voluntary to meet their common economic, social and cultural needs and aspiration through a jointly owned and democratically controlled enterprise. It is a business owned and democratically controlled by people who use its services and whose benefits are derived and distributed equally on the basis of use. The owners of the cooperatives are called members.

Cooperative is probably as old as civilization. Early people had to learn to work together to meet their common needs. In 1752, Benjamin Franklin organized the initial structured cooperative business, a mutual Fire Insurance Company in the United States. A group of 28 workers of the cotton mills in the town of Rochdale in the north of England established the first modern cooperative business, the Rochdale equitable pioneers society in 1844.

In Nepal, the cooperation had been evaluated in various senses from remote past. In 2010 B.S., the cooperative department was first established for the promotion of cooperatives, which started organized cooperative movement in Nepal. In 2013, formally organized cooperatives were established in Chitwan district by issuing executive order by the government. The first cooperative department was established in 2010 B.S. with the task to promote cooperatives followed by the first cooperative law in 2016 B.S.. A new law replaced this law in 2043 B.S. and again in 2048 B.S.. The later is currently operative. After the cooperative Act 2048 B.S., so many cooperatives have been established in Nepal.

According to the Department of Cooperative in Registered on July 2009 A.D., there are 12646 cooperatives involved in different sectors.

1.2 Focus of the Study

Mostly the Nepalese economy is rural based. Most of the people live in villages where the people are compelled to bear the high price of the goods and services and have no chance of using institutional credit at low rate. So, cooperative could be effective instrument to solve both the problems. This organization is regarded as the midway of capitalism and socialism. The farmers and small businessman and traders in the rural areas are not facilitated enough with banking services. So, in this context only cooperative can meet their requirements.

Cooperative Organization can be the most effective device for uplifting the socio-economic conditions of rural masses. Cooperative has been accepted all over the world as means for mobilizing the scattered savings and putting them in productive use for the benefit of the poorer section of the society. It helps to distribute wealth and profit equally to all the members of the society.

Financial viability of the cooperatives is essential requisite for their existence and long-term survival. Without financial viability they can not serve their members for long run and will become a burden to the society. Financial viability, strength and weakness of an organization can be measured / determined by analyzing of the financial statement. Performance indicators are usually calculated in the form of ratios and are compared over a period of time. Such trend analysis demonstrates whether financial and institutional performance is improving or deteriorating. This not only helps in monitoring and giving suitable solutions to deficiencies, but also in the planning, standardizing and supervisory control of the institutions. On the basis of a flexible systems and analytical framework, it is possible to monitor the complexity and dynamics of Micro Finance Institutions (MFIs) that in turn, facilitates in the credit ranking of such institutions.

Learning different methodology and applying them in operation is of dire to check the financial health of institutions. Many countries are applying new monitoring tools like CAMEL, IRDA, MCRIL, GIRAFE etc., which provide a supervisory control in the MFI operation and help to find the critical deficiencies faced by the institutions. Such tool gives the manager a clear direction in operating smoothly and promptly. The PEARLS, at recent times, have been developed by World Council of Credit Union (WOCCU) as a new tool that performs both the management and supervisory tools by regulators specifically for Credit Unions (CUs). The tools under PEARLS are applied to analyze the financial performance of Royal Cooperative Society Ltd. (RCSL).

This study basically focuses on the evaluation of the financial performance at finding the weak capital base and probable causes with the application of each of PEARLS tools. Using these tools helps the MFIs create universal language that every one can speak and understand. Further more, it brings MFIs in uniformity, which helps to rank the MFIs.

1.3 Statement of the Problem

Cooperative affairs the varieties of instruments, which have been applied in order to know the financial variability that in turn, determines the institution soundness. On closer examination, it is evident that these standard indicators are being calculated and applied in many different ways. This is a bit ambiguous among practitioners and analysts and gives considerable distortions when comparing MFIs. It is anticipated that using the methodologies that give a clear objective assessment quantitatively and bring every MFI under the same roof in terms of their performance is a crucial need that ranks the MFIs towards a better performance. Sometimes it goes far beyond in understanding the indicators that is to be clearly understood. However, the familiarity of the tool kits and its application might be helpful for the managers to identify the several panacea faced by the MFIs prior the implementation.

The major problem is how to analyze the financial performance of Royal Cooperative Society Ltd. in the framework of PEARLS

a. What is the protection level of assets?
b. What is the level of effective financial structure?

c. What is the scenario of assets quality?
d. What are the rate of returns on various investments and costs on saving deposits and external funds?
e. What is the level of liquidity and non-earning liquid assets?
f. What is the trend of growth in loan portfolio, liquid and financial investments, saving deposits, members share, institutional capital and total assets?

1.4 Objective of the Study

The major objective is to analyze the financial performance of Royal Cooperative Society Ltd., which is determined by the PEARLS tools.

Based on the major objective, the following specific objectives have been set.

a. To examine the protection level of assets.
b. To analyze the level of effective financial structure.
c. To asses the status of assets quality.
d. To evaluate the rate of returns on loan, financial and liquid investments and costs on saving deposits and external funds.
e. To assess the level of liquidity and non-earning liquid assets.
f. To analyze the trend of growth in loan portfolio, liquid and financial investments, saving deposits, members share, institutional capital and total assets.

1.5 Significance of the Study

This study will be more significance understanding the financial performance of the institution using the PEARLS tools. PEARLS monitoring systems use a set of financial ratios to the financial stability of institution. Such ratios provide the essential tools for monitoring, planning, standardizing, ranking and facilitating supervisory control. By using PEARLS tools, institution has to know its position in the market in terms of financial performance. This research will be more useful for the further research work in future.

1.6 Delimitations of the Study

This study has been undertaken only the financial aspect of RCSL in the framework of PEARLS. The analysis of the study is based on its annual reports and office report of the institution. The study has been made with reference to the periods of FY.061/62 to 065/66.

1.7 Organization of the Study

This study is divided into five chapters. The first chapter deals with Introduction, which consists of the background of the study, focus of the study, statement of the problem, objective of the study, significance of the study and delimitation of the study. The second chapter deals with Literature Review, which consists of the conceptual review and research review. In conceptual review, it is included concept of micro-finance, meaning and definition of cooperative, principles of cooperative, historical background and development of cooperative, organizational structure of cooperative, types of cooperative, concept of financial performance analysis, brief description of RCSL and theoretical perception of PEARLS framework. In research review, it is included review of articles and review of dissertations. The third chapter deals with Research Methodology, which consists of research design, justification for the selection of study unit, nature and sources of data, data collection method/procedure, data processing and analysis, PEARLS financial tools and limitation of the methodology. The fourth chapter deals with Data Collection, Presentation and Analysis and finally the fifth chapter deals with Summary, Conclusion and Recommendation.

CHAPTER TWO
REVIEW OF LITERATURE

This chapter consists the conceptual framework and research review and relevant theories for the analysis of the study. The former section presents the relevant aspects of the study and later on deal with research article in the related topics published in different national and international journals and review of dissertations studies by different authors.

2.1 Conceptual Review

This section comprises of general concept of MFI, concept of cooperative and its principle, historical background of Cooperative and its development in Nepal, organizational structure of cooperative and its existing situation, types of cooperative society, concept of performance analysis, description of RCSL Ltd and theoretical prescription of PEARLS. Review of research article includes the application of PEARLS tools to analyze the performance by different institutions in international scenario and the review of dissertation.

2.1.1 Concept of Micro-finance

Micro-finance plays a significant role in uplifting the economic condition of economically backward people living in the country. It is primarily concerned with credit and savings. Although, in recent times different allied services such as insurance, leasing, payment transfers and remittances are being introduced to mix. Finance services have proved the powerful instrument for poverty reduction, which enables the poor to build assets, increase income level and reduce their vulnerability to economic weaknesses. It is estimated that, as a region, South Asia has about 45 percent of all the people in the world who use micro-finance services in order to raise their living standards. [Patel, 2009:p.5]

However, with nearly one billion people are still lacking access to basic financial services, especially the very poor, the challenge of providing financial services to them remains. The goal of Micro Credit Summit Campaign (MCSC) is to reach 100

million of the world's poorest families with credit for self-employment and other financial and business services by 2005. According to MCSC authorized data in December 2003, the access of Micro Credit by 3164 Micro Credit Institutions have reached to 92,270,289 clients, among these people 66,614,871 were poorest people[Sam D. Harris,2005].

2.1.2 Meaning and Definition of Cooperative

Cooperation exists by live and let live. Cooperative is associated with human being in every stages of life. It may be compared with the company of birds, beats and insects. It teaches everyone to maintain disciplined life and coordination among each other. A cooperative organization is more guided by the service. It has render to the members than by the profit motive. It is completely differ from other forms of business organization.

The word "Cooperative" has been derived from the Latin word "Cooperate" which means in its ordinary sense working together but in broad sense, it means the system of people voluntarily associated working together in terms of equality to eliminate their economic exploitation by middlemen in respect to any exploitation others.

The International Cooperative Alliances (ICA) Continental meeting held at Manchester, England in 1995 defined "A Cooperative is an autonomous economic, social and cultural needs and aspiration through a jointly owned and democratically controlled enterprise"[NCD, 2054:p.75].

By the definition of International Labour Organization (ILO), it covered most of the principles of cooperation as such can be considered to the most comprehensive one. Cooperative society is "An association of the economically weak who voluntarily associating on the basis of equal right and equal responsibility transfer to an undertaking one for several of their functions, corresponding to one of several of their economic needs which are common to them all but which each of them is unable fully to satisfy by his own individual efforts and manage and use such undertakings in mutual collaboration to their common material and moral advantage" [B.P.Shrestha, 1984:p.115].

According to Maldenal, "They are association of persons, small producers or consumers who have come together voluntarily to achieve some common purpose by a reciprocal exchange of service through a collective economic enterprises working at their common risk and with resources to which all con but" [Puspa Ram Bhakta Mathema, 1969:p.153].

The progress of cooperative movement has been slow and in the some countries it is exceedingly slow. In the constitution of Nepal, it has been resolved to secure to all the citizens of Nepal justice, social, economic and political. As such cooperative societies have been given an important place in the constitution.

Economic development and social change are equally vital elements in the reconstruction of Nepal's socio-economic structure. Cooperation is one of the principal means for bringing about charges of a fundamental nature in the country. As such cooperative development has got priorities and various efforts have been made by the government through various economic plans to propagate the idea of cooperation in the country.

Financial cooperatives are non-profit making organizations established for the mutual benefit of the members. They are registered under the cooperative Act, 1992 at the respective District Cooperative Offices under the Department of Cooperative, Ministry of Agriculture and Cooperative and are allowed to accept deposits from and advance loans to their members only. They are authorized to carry on limited banking transactions among their members with prior approval of Nepal Rastra Bank (NRB).

Hence, the above given discussions concluded that cooperative is a form of organization specially of the weak and powers people where in actual users of certain goods and services voluntarily associate together as human beings, on the basis of equality for the promotion of their economic interest by honest means. Cooperation is the superior philosophy of life besides of a form of business organization.

2.1.3 Principles of Cooperative

Principles of cooperative refer to the guidelines to give the concrete form to the norms and values of cooperative organization. In other words cooperative principles are the set of rules and regulations to regulate and govern the activities of cooperative enterprise. The principles of cooperative are sociability and mutual aids the progress of organic life the improvement of the organism and the strengthening of the species, which become utterly incomprehensible.

The principles of cooperative have been given new dimensions from time to time to suit the changing environment and situation in order to make the cooperative movement more meaningful and purposeful. Due to rapid changes in the economy of the world, the need for review of the principle of cooperative was increasingly felt. In 1963, the International Cooperative Alliance had reviewed the existing principles. In 1995 September, the ICCA General Committee Meeting enunciated the following as the principles of cooperative [Cooperative Training Center, 2062:p.30]. Those principles have been commonly adopted all over the world.

1. Voluntary and Open Membership:- Cooperative organization is a voluntary organization. The membership of a cooperative society is open to all. It does not discriminate and show disparity to any one on the basis of caste, sex, politics and religious beliefs. Every body has the chance for free entry and exit to the members, which is set by cooperative acts.

2. Democratic Management:- To control and management of cooperative, organization is performed by its members through democratic system. All the members are eligible to participate in the policy making and decision making of the cooperative organization. Every member of the society should enjoy equal voting rights and participation.

3. Economic Participation by Members:- There is legal and equal economic participation of the members in this organization. They possess a common capital. A cooperative organization makes provision for reserve fund, dividend fund, patronage dividend fund, employees bonus fund, cooperative education fund and loss

compensation fund. The members of cooperative have opportunities to participate in economic activities. In this way, we find two kinds of economic participation of members in cooperative organization.

4. Limited Interest on Capital & Surplus Distribution:- Limited interest is paid on capital but the rates are varies from country to country. The interest, which is below the market rate, common benefit of the members being one of the fundamental principles, the profit earn by the cooperative society is distributed equally among the capital, labors and consumers.

5. Autonomous and Freedom:- Cooperative organization is an autonomous, independent and an organization controlled by its members. It is free from direct control of government and it does not make any agreement with the government or any other parties losing its autonomy democratic control.

6. Cooperation among Cooperative:- Cooperation among the cooperative is necessary for the smooth operation and all round progress of the cooperative movement. Mutual understanding and interdependence among cooperatives helps to the process of development of cooperatives. Cooperation develops closeness. Cooperatives are organized to each other to make the cooperative mission strong at the Local, Regional, National and International.

7. Self-help and Mutual help:- Cooperatives are not trade unions, charity or friendly societies. It is not a business but a combination of both business and social service. Cooperative evokes loyalty, sincerity and fellow feeling. The essence of cooperation is self-help unity, avoidance of competition and elimination of middlemen of all kinds in distribution and production. Cooperative works on the motto "Each for all and all for each". The feeling and the activities of the cooperatives helps us to stand on owns feet help to others and helps from others.

8. Education, Training and Information:- Cooperative launches training to its members, elected representatives and staff members. Cooperative education is necessary to make the members acquainted with the basic principles of cooperative

otherwise cooperative may die. For the qualitative management and development of cooperative organization, it should provide cooperative education, training and information to the members based on cooperative values and norms.

2.1.4 Historical Background

2.1.4.1 Global Prospective

In the early days in Great Britain, Cooperative movement contributed for the economic development. At the beginning of the 19th century, Robert Owen gave the idea of cooperative, but it was practically developed by a group of Rochedole Pioneers called the 'Consumers Society'. This was a successful cooperative society, which was started all over the Great Britain. In the beginning, this society sold goods only for its members but later it started to sell goods to non-members also.

Although, there have been in extend hundreds of societies but the truth is that it was the Rochedale Pioneers Society that achieved tremendous success and put economic and social life to Britain on the read of continuous progress.

In the world, the first cooperative college was established in 1919 in Manchester. The educational committee of the cooperative union and open administers it for the students from all parts of the world. After the achievement of cooperative society was recognized in 1944, the government of the Great Britain decided that boys and girls must attend a Country college after the learning school. The main motto was to produce good cooperative citizens within the Great Britain.

Cooperative is probably as old as civilization. Early people had to learn to work together to meet their common needs. In 1752, Benjamin Franklin organized the initial structured cooperative business, a mutual Fire Insurance Company in the United States. A group of 28 workers of the cotton mills in the town of Rachdale in the north of England established the first modern cooperative business, the Rachdale equitable pioneers society in 1844 (ICA, 2005a).

2.1.4.2 History and Development of Cooperative in Nepal

The word "Cooperative" and its concept is not a new. Everyone has already familiar for about its concept and principles. Self-help, mutual help and cooperation are in practice among the people from the very ancient times. Concept of cooperative is developed with the development of human civilization. Getting together with a view to helping each other or social occasions like marriage, shradha and other performing agricultural activities like plugging, sowing, crop protection, harvesting is a traditional of doing thinks in the rural mountainous and even the growing urban areas of Nepal. The different types of cooperative societies DHIKURI, PRAMA, GUTHI and MANKAKHAL are used in practice in Nepal from the ancient time.

The concept of cooperative in Nepal is not a new one. It is familiar from those days when people had the knowledge to live together in a society or community. But we can't ascertain the actual date when the cooperative movement was started in Nepal. Many types of informal cooperative were running in different parts of Nepal but those are not in a position to take formal slope of cooperative. If, we turnover the history of cooperative movement of Nepal, the organized history can be traced back to about 54 years old. Formally, the history of Nepal has been started after the establishment of cooperative development in the year 1953 under the Ministry of Agriculture for the promotion, supervision and evaluation of cooperative societies.

In the beginning, cooperative movement was greed up with the establishment of 13 credit cooperative societies in 1956 as part of the resettlement program for the flood stricken people in Rapti Dum Besi under the active support of United States Agency for International Development (USAID) on experimental basis. These cooperatives were previously registered under an executive order of government of Nepal.

The history of cooperative society dates back to 1956 A.D. in which year then the government incorporated Bhakhan Saving and Credit Cooperative Ltd. In Rapti Valley, Chitawan by issuing executing order for its legal validity [Keshar J. Baral, 2005]. The Thirty-year Panchayat regime also attempted to promote cooperatives by enforcing the cooperative Act, 1959 (2016 B.S.) and Cooperative Regulation, 1961 (2018 B.S.).

However, cooperative became burdensome to the government due to the weak management, want of autonomy and unscientific accounting system of saving and credit. After the restoration of democracy in 1990 (2047 B.S.), then the government considered cooperatives as a means of poverty alleviation.

Table 2.1: Major Events of Cooperative Movement in Nepal

Year	Event of Cooperative Movement
2010 (1953)	Establishment of Cooperative Department under the Ministry of Plan Development and Agriculture
2013 (1956)	Issue of executive order for the legal recognition of Cooperative Society in Chitwan District
2016 (1959)	1. Cooperative Development transferred under the Ministry of Food, Agriculture & Forest 2. Issue of Cooperative Act, 2016
2018 (1961)	1. Issue of Cooperative Regulation, 2018 2. First Amendment of Cooperative Act, 2016 3. Establishment of Cooperative Development Fund 4. Establishment of Sajha Sanstha Ltd.
2019 (1962)	1. Establishment of Cooperative Training Center 2. Establishment of Cooperative Exchange and Loan Association 3. Issue of Cooperative Bank Act, 2019 4. Cooperative Department transferred under the Ministry of Panchyat
2020 (1963)	1. Establishment of Cooperative Bank 2. Cooperative Section had been kept under the District Panchyat
2021 (1964)	Beginning of Agriculture Re-organization Program
2023 (1966)	Cooperative Department had been transferred under the Ministry of Land Reform Agriculture & Food
2024 (1967)	1. Formation of Central Investigation Committee for Cooperatives 2. Cooperative Bank transferred into Agricultural Development Bank
2026 (1969)	1. Cooperative Department transferred under the Ministry of Land Reform 2. Operation of Cooperative Agriculture Development

3. At first, Compulsory Savings (Anibarya Bachat) converted into share of Cooperative Societies, Bhaktapur
4. Cooperative Exchange & Loan Association changed into District Cooperative Association

2027 (1970)
1. Second Amendment in Cooperative Act, 2016
2. Arrangement of Central & District Cooperative Improvement Committee.
3. The Management of Cooperative Societies transferred to the Agriculture Development Bank

2028 (1971) First Amendment of Cooperative Regulation, 2018

2029 (1972) Operation of Regular Cooperative Education Program

2033 (1976)
1. Beginning of Population Education through Cooperative
2. Occurrence of Central Sajha Development Committee
3. Second Amendment of Cooperative Regulation, 2018
4. Compulsory Savings converted in to the share of Sajha

2034 (1977) Fiscal Regulation, 2034 issued for the Sajha Society Management

2035 (1978)
1. Management of Cooperative again transferred to Operating Committee from Agriculture Development Bank
2. Issue of Fiscal & Administrative Regulation for Cooperatives

2041 (1984) Issue of Sajha Society Regulation, 2041

2043 (1986)
1. Conducted the National Cooperative Seminar
2. Issue of Sajha Society Regulation, 2043
3. Cooperative Department changed into Sajha Development Department
4. Cooperative Training Center changed into Sajha Development Department
5. Regional Cooperative Offices changed into Regional Sajha Development Offices
6. Cooperative Branch Offices changed into Sajha Development Branch

2044 (1987) 17 members high-level Central Coordination Committee formed for the Effective Development of Sajha Movement

2045 (1988) Announcement to return of Compulsory Saving to the savers

2046 (1990)	Formation of Adhoc Committee for the formation of Central Sajha Society
2047 (1991)	1. Formation of 7 members Central Cooperative General Association Consulting Committee & the committee submitted its report 2. Conducted the Seminar on National Cooperative Development
2048 (1991)	1. Dissolved the Sajha Central Office 2. Established the 11 members National Cooperative Development Board
2049 (1992)	1. Issue of Cooperative Act, 2048 2. Formation of District Cooperation Committee and Cooperative Adhoc Committee 3. Sajha Development Department transferred into Cooperative Department 4. Sajha Training Center transferred into Cooperative Training Center 5. Regional Saha Branch changed into Regional Cooperative Office 6. Sajha Development Branch changed into District Cooperative Office
2050 (1993)	1. Issue of Cooperative Society Regulation, 2049 2. Nationwide election conducted of Cooperative Organizations 3. Formation of National Cooperative Federation 4. Establishment of Central Cooperative Federation 5. Establishment of National Saving & Credit Cooperative Federation 6. Establishment of Nepal Federation of Saving & Cooperative Union Ltd. 7. Establishment of Central Dairy Cooperative Federation 8. Establishment of Consumer Saving & Credit Cooperative Societies at a large scale all over the country
2052 (1995)	Formation of high-level Cooperative Improvement Committee & the committee submitted its report
2057 (2000)	1. First Amendment of Cooperative Act, 2048

2. Formation of the National Cooperative Development Advisory Working Team & the team submitted its report

2058 (2001)
1. Announcement of observance of International Cooperative Day by the Government
2. Republication of "Shahakari Sandesh" weekly

2059 (2002)
1. Cooperative Ministers' Conference hosted by Nepal organized by International Cooperative Alliance (ICA), Regional Office for Asia and the Pacific, New Delhi in collaboration with National Cooperative Federation of Nepal.
2. The Ministry of Agriculture and Cooperatives has issued a circular, saying that there is no restriction for the eligibility of 'Civil Servant' as shareholder of cooperative although the Sec.14 of the Anti-corruption Act refers to civil servant not eligible to become the shareholder of cooperatives
3. Nepal elected for the member of ICA ROAP Standing Committee

2060 (2003)
1. Establishment of National Cooperative Bank Ltd.
2. Seventh General Assembly of Network for Development of Agricultural Cooperatives (NEDAC) was held in Nepal from 29th Oct. to 1st Nov. In which Nepal was elected as Co-Chairman for two years.

2061 (2004)
1. National Cooperative Federation of Nepal established "National Cooperative Development Fund" (NCDF).
2. Nepal Government constituted a high-level cooperative sector improvement consultative committee under convenorship of the Ministry of Agriculture and Cooperatives submitted its report to the Government of Nepal.
3. Government of Nepal announced the policy of GOAN GOANMA SHAHAKARI GHAR GHARMA ROJGARI through its budget of the current fiscal year 2061/62

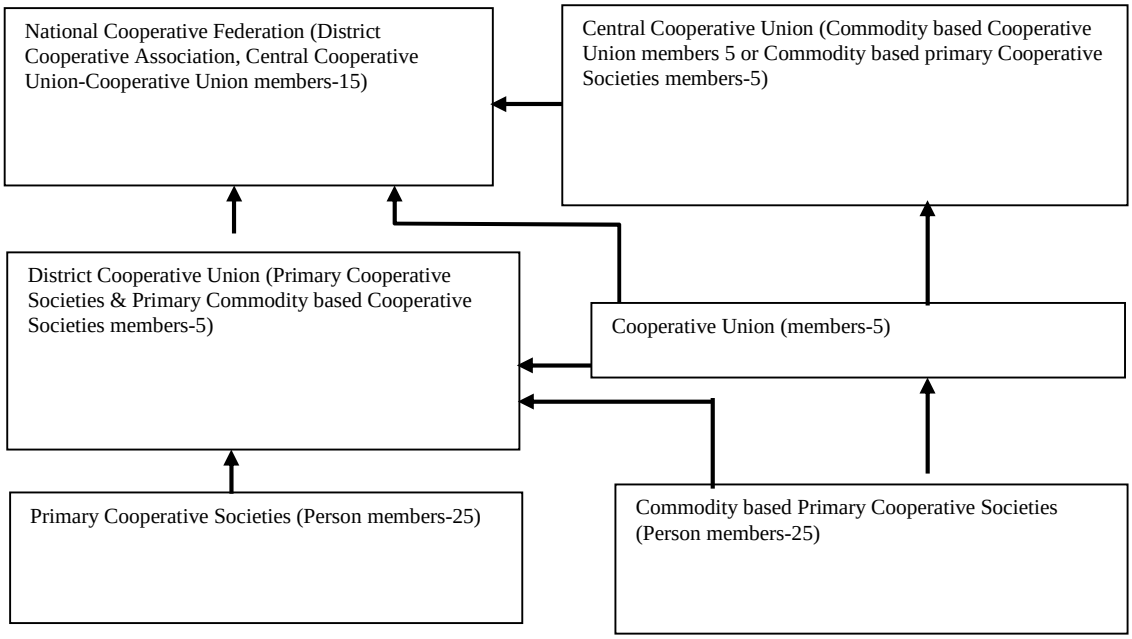
2062 (2005)
1. Completion of Second National Women Cooperative Congress held at Kathmandu.
2. Change of name of MOAC
3. Change of name of CTC into Central Cooperative Training Center

	4. Change of name of District Cooperative Office into Division Cooperative Office. 5. Establishment of Regional Level Cooperative Training Office combining with Division Cooperative Office in Kailali, Surkhet, Kaski and Chitwan.
2063 (2006)	1. Change of Agriculture Policy Unit into Agriculture and Cooperative Policy Unit in MOAC for coordination and establishing contact about cooperative policy making. 2. Election of Nepal as Standing Committee Member of ICA/AP 3. Establishment of Central Coffee Producers Cooperative Union 4. Establishment of Central Fruits and Vegetables Producers Cooperative Union. 5. Election of Nepal as Vice-chairman of Housing Cooperative Foundation. 6. Beginning of Cooperative Golden Jubilee 2006/07 throughout the country for full year
2063 (2007)	Completion of Cooperative Golden Jubilee 2006/07 with four special cooperative publications.
2064(2008)	Issuing Standards of Registration and Renewing Process to co-operative societies and unions.
2065(2009)	Modifying to Issuing Standards of Registration and Renewing Process to co-operative societies and unions of 2064(2008).

The above activities during last 53 years in the history of cooperative movement in Nepal are enough to say that cooperative development passed through many managerial ups and downs causing a high inconsistency. The cooperative movement remained affected by the political changes in the nation that brought the situation among the people not to believe readily in the philosophy of cooperative in practice. Moral objectives, social obligation, service to members, good quality, cheap pricing, reasonable profit, cooperative principle have been the major challenges for cooperative organization in the present context of competitive market.

2.1.5 Organizational Structure of Cooperatives

There is a provision clearly stated according to Cooperative Act, 1992 clause 3.1, cooperative organization can be established for economic & social development for its members as per the cooperative principles. Cooperative Act, 1992 has the provision of three-tier system for agricultural cooperatives and four-tier system for non-agricultural cooperatives. The organizational structure of the cooperative organization is as follows.



Primary cooperative is formed with 25 members where as secondary level or district level union is the secondary tier formed with the affiliation of at least 5 primary cooperative societies. It provides necessary services needed by the members by coordinating its member's societies. Central cooperative union is a central level union of the commodity based primary societies or and district unions, which is responsible for promotion, education, coordination and training activities for its members. Central cooperative union can be formed with the affiliation of at least 25 single purpose cooperative societies or 5 district cooperative unions of the same nature.

The last and the higher tier of the cooperative is the National Cooperative Federation, which is a national level organization of all types of cooperatives. It is formed with the affiliation of all the unions with the minimum number of 15 unions.

Existing Situation of Cooperative

The existing situation of cooperatives in Nepal (up to 2066) is as follows;

1. Division Cooperative Office - 38
2. Cooperative Societies Operating District - 75
3. National Cooperative Federation - 1
4. Subject-wise Cooperative Central Union - 5
5. National Cooperative Bank - 1
6. District Cooperative Union - 51
7. Subject-wise Cooperative District Union - 87
8. Primary Cooperative Societies - 12646

Table 2.2: District Cooperative Union (Kaski District)

S.No.	Particulars	No. of Cooperative	Share Capital	Members
1	Multipurpose	26	20898000	10346
2	Science & Techno.	4	50000	104
3	Saving & Credit	126	226026000	24423
4	Agriculture	33	3806000	2953
5	Dairy	28	2663000	2102
6	Coffee	6	108000	169
	Total	**223**	**253551000**	**40097**

Source: **Cooperative Department (District Profile)**

Table 2.3: Primary Cooperative Societies

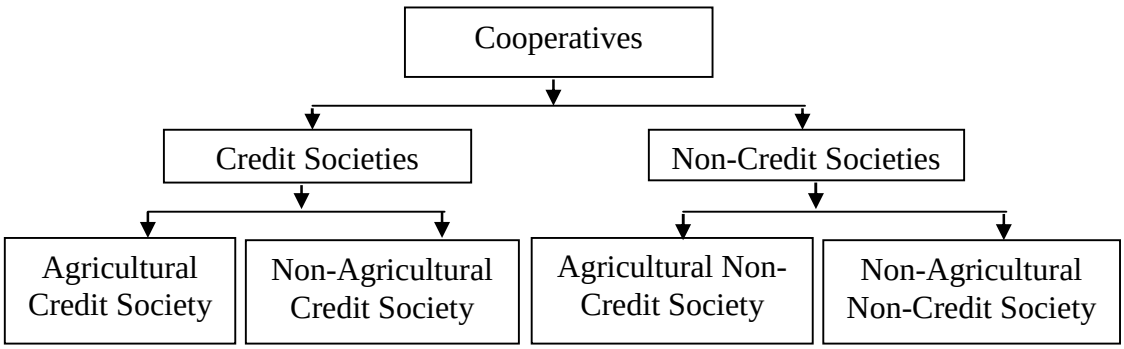
S.No.	Particulars	No. of Cooperative	Share Capital (NRs.'000)	Members	
				Male	Female
1	Saving & Credit	5162	2191126	401719	312797
2	Multipurpose	2978	1252501	447626	157935
3	Dairy	1603	50395	68560	26738
4	Agriculture	1736	185747	230129	91369
5	Vegetable & Fruits	123	2713	4582	3353

6	Electricity	257	6531	13415	2458
7	Consumer	201	15892	7002	2087
8	Science & Technology	83	59656	6304	1171
9	Coffee	73	896	1288	775
10	Health	41	113841	3696	482
11	Herbal	38	2645	1276	381
12	Tea	48	5826	1219	699
13	Others	273	5070980	24832	30854
	Total	**12616**	**8958749**	**1211648**	**631099**

Source: **Cooperative Department Statistical Description Profile, 2066**

2.1.6 Types of Cooperative Societies

Cooperative has been considered as a life style under which people work together for common economic & human interest. Cooperative has different types as per its purpose. Cooperative credit societies are further classified into agricultural credit societies and non-agricultural credit societies. Non-credit societies are classified into agricultural non-credit societies and non-agricultural non-credit societies. This can be clearly shown from the following chart.



The Agricultural Credit Society is formed in the rural area among the farmers to avail short-term loan to farmers and promote their savings where as the Non-Agricultural Credit Societies are formed in the urban areas. Urban banks, life insurance societies, salary earner's societies, fisherman's societies, consumer's cooperative societies, industrial cooperative societies and cooperative housing societies are the prominent non-agricultural credit societies.

The major types of cooperatives in Nepal are as follows.

1. Multipurpose Cooperative Societies:- Multipurpose Cooperative Societies render their services through different channels in different fields and their aim is an all round economic development. There are 2978 multipurpose cooperative societies in Nepal up to end of Chaitra, 2065.

2. Saving & Credit Cooperative Societies:- Saving & Credit Cooperative work for promoting the savings of the people, collecting such savings and granting loan to the members for different productive business at low rate of interest. In Nepal, where people have low income level, spendthrift and suffer from the exploitation of private lenders, such cooperatives are very important for the uplifting the economic condition and life style of those people. After the enactment of Cooperative Act 2048, a number of credit & saving cooperatives have been established and they are increasing day by day. The no. of saving & credit cooperatives has reached 5162 up to end of Chaitra, 2065 in Nepal.

3. Milk Producer's Societies (Dairy Cooperatives):- Being a mountainous country with grassy land, Nepal has a high prospect of dairy products. In this context, milk producer's societies or dairy cooperatives can play the vital role for material development by helping the milk producers in their business. There are 1603 no. of dairy cooperatives in Nepal up to end of Chaitra, 2065.

4. Consumer's Cooperatives:- Consumer's Cooperative eliminate the exploitation of middlemen upon consumers. Consumers cooperatives are established by consumers not to suffer from the problems like under weighting adulating of foodstuffs, artificial boosting up of prices of commodities etc. Such societies have been very common in Nepal. The no. of such consumer societies had reached 201 up to end of Chaitra, 2065.

5. Agriculture Cooperative Societies:- Agriculture is the backbone of economic development of Nepal. To develop the economic condition in Nepal, aggregate scientific agricultural system should be conducted. Agriculture Cooperative Societies have objective to provide the agricultural instruments & tools, improved seeds,

fertilizer to the farmers at reasonable price. Now, the no. of agriculture cooperative has reached 1736 up to end of Chaitra, 2065.

6. Cooperative Marketing Societies:- The Cooperative Marketing Societies encourage farmers to produce more and help them for marketing their products at reasonable prices. They save farmers from the exploitation of private profiteers. In Nepal, though there are some such cooperatives working but they are suffering from transport facilities, scarcity of capital & lack of trained persons.

7. Cottage Industrial Societies:- Cottage Industries play significant role for economic development in the country. These societies are established for facilitating the cottage industries for raw materials, equipments, marketing & so on. Such cottage industrial societies are organized in different parts of country e.g. Tansen, Dhankuta, Ilam, Patan, Banepa, Birganj, Pokhara etc.

8. Others:- There are other cooperatives of different kinds in different sectors such as poultry farming societies, Tea & Coffee, Herbal, Science and Technology, women's cooperative, small farmers, Electricity, Health etc.

2.1.7 Brief Description of Royal Cooperative Society Ltd.

Royal Cooperative society was established in 8th Jestha 2059 according to Nepal Government Cooperative Act 2048. Only by 28 members being started in establishing period of this cooperative has 808 members till now (FY 066/67). The main objective of this cooperative has to provide the financial services to the poor farmer groups, labour groups and low capital holding groups that are ignored by public and private bank and financial institutions.

2.1.8 Theoretical Prescription of PEARLS Framework

PEARLS is a set of financial indicators and management tool that help to standardize terminology between the institutions [Anna Cora Evans and Brian Branch, 2009]. It is also a supervisory tool for regulators. It can be used to compare & rank institutions, it can provide comparisons among peer institutions in one country or across countries. The PEARLS system was originally designed and implemented with Guatemalan CUs

in the late 1980s [Anna Cora Evans, 2007 (magazine no. 37)]. PEARLS provide a systematic approach to develop strong modern CUs that balance the needs of savers, borrowers, stakeholders and staffs. It has proved a key tool in achieving CUs growth & self-sustainability. The purpose for including a myriad of indicators is to illustrate how to change in one ratio has ups hot for numerous other indicators. Each indicator has a prudential norm or associated goal..

PEARLS provides MFI managers with concise, easy to read reports that reveal institutional weaknesses and trends. It also offers a strategic business-planning tool to help managers implement change. PEARLS indicators show the adequacy of CUs delinquent loans provision, how close CUs were to international CU capital structure standards, the excess non-performing assets, the income and cost yields, the management's cash administration abilities and the growth in key operational areas [Brian Branch and David Richardson, 2009].

PEARLS methodology can be applied to MFIs in order to find key areas of its operations both in terms of financial structure and growth. As a managerial tool, it helps to the MFIs to monitor and improve their performance. WOCCU and its member countries are using these tools to monitor, supervise and check up the financial health of MFIs like Credit Unions and Cooperatives.

The important realization from the use of PEARLS is the provision of framework for a management and supervisory tools that goes beyond the simple identification of problem. It identifies the weak capital base of MFI and its probable causes thereby giving the meaningful solutions to serious institutional deficiencies by using the PEARLS monitoring system. Further, the use of standardized financial ratios under this system eliminates the diverse criteria used by the MFIs to evaluate their operation. National Associations can be use the financial ratios generated by PEARLS to conduct quarterly or monthly analysis of all key areas of MFI operations that determines the performance of MFI. These evaluations are invaluable for spotting trends and detecting areas of concern among the affiliates.

Considering the assets growth of institutions is much horrible and one of the key strategies to address the problems that accompany monetary devaluation and runaway inflation. Financial institution has to sustain the aggressive growth to preserve the value of the assets in the hostile macro-economic environment. As it has been already referred each of the letter of PEARLS, the first and foremost is the evaluation of asset indicators to ensure that the financial institution provides depositors a safe place to save their money with the standard of excellence.

2.1.8.1 Protection (P)

Protection defines to protect the members from losing their amount of savings made at the institution. Protection is very crucial component, which refers to the safe of money of the member-client of MFIs. It is remarkable that every client should be member. Anybody else can open the saving account and borrow the money only after receiving membership of the cooperative. So, every member is the client & every client is the member of a cooperative. Unless & until potential member-clients do not feel safe to deposit their money in a cooperative, they do not deposit their savings. It is the provision of allowances to cover the loan losses resulted from the loan delinquency. Delinquencies occur when the debtors become unable to repay the loan principal amount in prescribed time. When more delinquencies exist, then the performance gets slithered as a result of a greater loss.

Since, the institutions heavily depend upon providing the loan in different assets comprising a slightly higher interest rate. Provisions for loan losses are the first line of defense against unexpected losses to the institutions. Allowances for loan losses are essential since delinquency signals that loans are at risk. Thus the institutions must set aside earnings to cover these possible losses to protect the member-client savings.

According to the WOCCU model, protection against loan losses is deemed adequate if a cooperative has sufficient provision to cover 100 percent of all loans delinquent for more than 12 months and 35 percent of all loans delinquent for 1-12 months [David C. Richardson, 2009]. In Nepal, Cooperative licensed for limited banking services; collection of saving and lending the money should have 1 percent of Pass loan (loan & advances not past due and past due for maximum 3 months), 25 percent

of Substandard loan (loans & advances past due 3 months to 9 months), 50 percent of Doubtful debt (loans & advances past due 9 months to 1 year) and 100 percent of Bad debt (loans & advances past due more than 1 year) for loan loss provision [Nepal Rastra Bank, 2002]. But thousands of Saving and Credit Cooperatives are out of the jurisdiction of NRB. So, most of the cooperatives do not have loan loss provision as per this directive.

The PEARLS system evaluates the adequacy of protection afforded to the cooperative by comparing the loan loss provision to amount of loan at risk. In this system, loan loss provision is considered as the first line of defense against non-performing assets. The degree of protection is measured by six different ratios.

2.1.8.2 Effective Financial Structure (E)

Effective Financial Structure refers to the composition of different sources of resources. It includes short-term debt and long-term debt as well as shareholders equity. The evaluation of financial structure of the balance sheet is a critical area of concern in many countries since the modernization implies a major restructuring of financial institution's assets, liabilities and capital. Balance sheet structure has a direct impact on efficiency and profitability and these areas are critically important for effective and sustainable MFI operations in a competitive environment.

PEARLS monitoring system measures the effective financial structure focus in both financing of resources and effective use of the resources like loans, investments, deposits, shares and institutional capital of MFIs. An institution has an effective financial structure when assets financed by savings deposits, generate sufficient income to pay market rates on savings, cover operating cost and maintain capital adequacy [Anna Cora Evans and Brian Branch, 2009].

The PEARLS monitoring system measures assets, liabilities and capital and thereby recommends an ideal structure for CUs. The indicators under effective financial structure help to optimize institutional solvency, profitability and liquidity. It encourages community loans to members, community savings from either rich or poor members and capital accumulation through earnings instead of member's shares.

According to PEARLS system, investment in net loan, liquid assets, financial assets and non-financial investments should be in the range of 70 to 80 percent, 20 percent, 10 percent and zero percent of total assets respectively. This implies that MFIs should not invest in non-financial assets such as supermarkets, pharmacies, residential housing development etc. Financing of total assets with saving deposits, borrowed funds and member share capital should not exceed 80 percent, 5 percent, and 20 percent of total assets respectively. Institutional capital should not be at least 10 percent of total assets of MFIs [David C. Richardson, 2009].

Institutional capital comprises of regulatory resources, other resources, monetary donations and grants and undivided earnings. In the case of cooperatives, ownership

share capital is not included in the institutional capital. Share capital is withdrawable upon the termination of the membership and in some cases it is used to secure the loan. The ratio of institutional capital to total assets measures the capital adequacy of MFIs. It should not come down at least below 10 percent of total assets [WOCCU, 2009].

2.1.8.3 Asset Quality (A)

Asset quality means the capacity of assets that generate income as well as the recoverability of the principal amount as per their prescribed terms and condition. The quality of assets would depend largely on the risk management system of institution. An excess of defaulted or delayed repayment of loans and high percentage of other non-earning assets have negative effects on institution's earnings because these assets are not earning income. Loan and advances dominate the asset side of the balance sheet of any financial institution. Asset quality measures how effective an institution is at lending money to people who are willing and able to repay promptly from the income generating as a result of investing in the productive sectors.

Quality of asset of cooperative affects its earning power. Investment in non-earning assets and increase in the assets at risk deteriorate the earning power of a cooperative, decrease the institutional capital and finally lead it to the liquidation.

PEARLS uses these three indicators; delinquency ratio, percent of non-earning ratio and financing of non-earning assets to identify the impact of non-earning assets [David C. Richardson, 2009:p.4]. Delinquency ration measures the delinquency rate of the total loan portfolio. It is commonly referred to as portfolio at risk, is the total outstanding balance of loan delinquent greater than 30 days. It is the most important indicator of the quantity of assets. This ratio is a measurement of institutional weakness because if delinquency is high, then other key areas of institution operations could be weak. Institution depends upon investing the saving deposits in the quality of assets, which inherently possess risk though it generates a higher income compared with other investments. The higher delinquency ratio implies more severity in the financial condition and presence of higher risk to the member-client savings. This ratio should not exceed 5 percent of the total gross loan portfolio.

The non-earning assets are those assets, which do not generate income. These non-earning assets are cash at hand, non-interest bearing monetary checking accounts, account receivable, assets in liquidation, fixed assets (Land, Building, Equipment etc.) and prepaid expenses and other deferrals. The assets quality measures the percentage of investment of MFIs in non-earning assets. Sometimes, MFIs have to invest their funds in such assets to improve their physical image and attract more new member-clients, increase the member share capital and saving deposits, and finally increase the total assets. Institution needs to reduce the percentage of non-earning assets through considerable level of retaining the fixed assets. Institutions may face another acute problem when they finance in the purchases of fixed assets with member shares. All these result, in the low percent of investment in non-earning assets in the long run. Thus, increase in the percent of non-earning assets should be temporary. Total investment in non-earning assets of MFIs should not exceed 5 percent of their total assets.

Traditionally, CU uses member share capital to finance the purchase of fixed assets. Under the WOCCU model, the objective is to finance 100 percent of all non-earning assets with CUs institutional capital. It can also finance with other liabilities that bears no explicit financial cost. The institution earnings are less affected by using such capital to finance the purchase of fixed assets.

2.1.8.4 Rates of Return and Costs (R)

The Rates of Return and Costs indicators monitor the return earned on each type of assets and the cost of each type of liability. On the assets side, one can determine what types of assets earn the highest returns. On the liability side, one can determine what the least and most expensive sources of funds are. Yields and Costs directly affect the growth rates of an institution.

PEARLS system segregates the different components of yield on investment and evaluates the efficiency of management in terms of investments by comparing the yields on different components of the investments and identifies the problem area of operational cost of MFIs.

Yield is computed in four main areas; loan portfolio, liquid investments, financial investments and other non-financial investments. And the cost is broken down into three main areas; financial intermediation costs, administrative costs and unrecoverable loan costs.

The 'R' category also measures operational costs including financial cost paid on deposit savings, share savings and internal loans. The income ratios identify income from loan portfolio, liquid investments, financial investments and non-financial investments. These indicators, which generate income, are to be considered under the rate of return. These indicators help to optimize the balance between portfolio yields, saving deposit yields, dividend on shares, operating efficiency and the capitalization of net earnings.

In general, the WOCCU model compares the calculated returns to the entrepreneurial returns and market rate of returns. In the same vein, cost of the funds like cost of the funds raised from the saving deposits, external credit, cost of member share capital also is compared with the market rates. Thus, this component evaluates the yields on the investment and financial costs paid on member savings, member shares and external loans [Keshar J. Baral, 2006, p.45-69].

2.1.8.5 Liquidity (L)

Liquidity is an essential component of administering saving institutions. It is necessary to respond to member-client withdrawal and disbursement demands. The institution should manage the availability of liquidity reserves as the member shares are illiquid and most external loans have a longer pay aback period. Maintaining the high liquidity affects the profitability adversely. Since, investment in the liquid assets yields very low rate of return. Some of the liquid assets such as cash on hand and checking account yield nothing at all.

Traditionally, liquidity is viewed in terms of cash available to lend in a financial institution. Lending in a financial institution is a variable under the control of the management of an FI. But bringing about the withdrawable saving deposits in an FI

has added the new dimension to the concept of the liquidity. In this perspective, liquidity implies the cash required for possible withdrawals of saving deposits.
The adequacy of cash reserves to satisfy deposit withdrawal requests is measured. PEARLS system uses two ratios: liquidity reserve to saving deposits and non-earning liquid assets to total assets.

2.1.8.6 Sign of Growth (S)

Sing of Growth refers to the member-client satisfaction, appropriateness of product offerings and financial strength. Growth of assets accompanied with sustained profitability is to the successful MFIs. Growth is measured in these key areas: total assets, loan, liquid investment, financial investment, saving deposits, external credit, member share capital, institutional capital and number of members. Growth in total assets is one of the most important ratios. Strong and consistent growth in total assets brings about the improvements in many key ratios. Annual growth rate should be more than inflation rate.

Loan portfolio, is another most important assets of FIs. Growth in total loan should keep the same pace of the growth in the total assets. Lower growth in total assets implies the investment of funds in less profitable assets and conversely the higher growth in loan portfolio signals good probability of maintenance of profitability. Growth in saving deposits affects the growth in loan portfolio and total assets. It affects other key areas of MFIs positively. But high growth in saving deposits may be turned out burdensome if MFIs is not able to mobilize the deposits to profitable investment.

Growth in institutional capital reflects the profitability of MFIs. It is difficult in adding to institutional capital for an MFI with low earnings. Constant growth rate or declining growth rate indicates a problem with earnings. Sustainable institutional capital growth rate, usually, greater than the growth in total assets shows the robustness of an MFI. In this section, the different 11 indicators measure the percentage of growth.

2.2 Research Review

Research review deals with the review of articles published by different authors in international scenario and review of dissertation written by different authors. The articles and case study in PEARLS are extracted form the official websites of WOCCU Inc., ABCUL Credit Unions, Banking with the poor (BWTP), the Micro Banking Bulletin (MBB) and the BASIS Collaborative Research Support Program (CRSP). The review of dissertation is made by with respect to various authors for their master degree course visiting in Central Library, Kirtipur, Kathmandu and Western Library, Pokhara.

2.2.1 Review of Articles

Branch and Richardson undertook a monograph work in Ecuador credit union micro-enterprise innovation project [Brian Branch and David Richardson, 2009]. The ongoing project was designed to be a technical assistance and training program. The WOCCU worked with 19 CUs and this monograph evaluated the project's impact in four areas CU's membership, CU financial supervision and governance policies, CU's savings deposits and lending services and CU's financial performance.

Almeyada and Branch carried out a case study on measuring sustainability: Financial and Operational Performance of two CUs namely; Union Popular (UP) and Union Progresista Amatitaneca (UPA) based on PEARLS monitoring system for the periods 1994, 1995 and 1996 [Gloria Almeyada and Brian A. Branch, 2009]. They applied 25 indicators as a monitoring tool under PEARLS to monitor the comparison of these two CUs. The study focused in building the institutional base and growth of total assets with reliance in savings and deposits. In addition to it, the provisioning of allowance against the loss assets was also the attention they had paid for. The study exhibited that the UPA was able to generate more institutional capital than UP, a part of strategy to build a more solid capital base. But, contrary to the PEARLS standard, UPA heavily relied on member shares rather on savings deposits, which UP was strictly adhering. In conclusion, the study revealed that the application of tools helped the both institution to build a stronger base for their performance.

Sasuman undertook the case study on Rural Financial Institutions: Restructuring and Post Restructure Results while working in Credit Union Empowerment and Strengthening (CUES) Philippines[Luis Sasuman, 2009]. CUES Philippines actively utilized the PEARLS Monitoring System's 46 financial ratios to enable Batch 1 partner cooperatives and monitor their overall financial position. His case study was based in reference to two years break i.e. 1998, 2000 and 2002 using PEARLS ratios. The goal of the project is to improve the performance of credit cooperatives and provide financial services to the segment of the population that do not have access to credit or any other financial services. It partnered and worked on the transformation of eleven credit cooperatives known as Batch 1 from Mindanao. The case study describes the CUES Philippines project, a combination of two methodologies: Model Credit Union Building and Savings and Credits with Education. The project's success in strengthening and empowering credit cooperatives shows that the two methodologies, when provided together, can increase member income and savings and empower women.

Evans undertook a case study on strengthening WOCCU's partners in a time of crisis using PEARLS financial monitoring in Ecuador[Anna Cora Evans, 2001]. This monitoring system was applied as a tool to monitor and improve their performance. In this case, 12 indicators of PEARLS were applied to monitor the performance. However, the growth in membership and institutional capital with a prime focus in savings deposits was a goal of the institution which it has to some extent, attained.

Winkworth applied the PEARLS technique in Portsmouth Savers Credit Union when it joined first ABCUL/Barclays PEARLS Project[Amanda Winkworth, 2009]. With initial start up grant funding and a citywide common bond, the CU had one office with two members of staff and had gained nearly 1000 members. At that time the level of expenditure was seven times larger than the income in a year. Working with PEARLS led the staff and board of credit union to see that it was not competitive in the market place. They realized that they needed to make major changes to their policy to enable them to earn enough money to make the business viable when they start up funding came to an end. The CU introduced capacity based lending with focusing the members who apply for loans were now judged purely on their ability to

repay the loan and not on their previous saving record with the CU. PEARLS revealed the CU that the satisfaction of savers was equally important. In the three years since PSCU started working with PEARLS, membership has more than tripled to over 2800 and savings were also trebling of the previous PEARLS figure. The CU has a loan portfolio more than four times the amount before the CU introduced the capacity based lending.

2.2.2 Review of Dissertations

Ale conducted a research with the objective of diagnosis the financial health of Paschimanchal Gramin Bikas Bank Ltd. in the framework of PEARLS with the help of secondary information using PEARLS tools[Hum Bahadur Ale, 2007]. The major finding from his study were able to allocate the allowance for loan losses, maintaining non-earning liquid investments up to its standard, lower the operating expenses consecutively over the periods, the institutional capital has not been attained up to its norms. This is due to the poor assets, which have been fallen in high delinquency and able to attract more deposits so as to augment the total assets. The poor in savings to invest in quality loan portfolio and delinquency has resulted sternly from earning or significant level with respect to PEARLS standard. the institution in the event of focusing primarily in savings deposits to invest in quality loan portfolio will substantially add up the institutional capital as a result of yielding earnings that shall eventually ensures the sound financial health of Paschimanchal GBB Ltd. He recommended that the institution to focus on the saving deposits as the main source of growth in total assets and develop an effective marketing program to attract more savings.

Lamsal conducted a research with the objective of examining the financial variability of association whether they are financially sound or not with the help of secondary information as well as primary[Toya Nath Lamsal, 2000]. The major findings from his study were satisfactory liquidity position, inefficient management, un-trend turnover ratio, unsound capital structure, unable to mobilize its funds in profitable sectors, unsatisfactory return on assets and capital employed, unable to utilize its assets capacity, inconsistent credit policy, negligible share capital in terms of financial standard limits. The overall financial performance of the association is very weak. He

recommended that the association is required to improve the management and adopt the appropriate financial policy otherwise it may fall in crises.

Prem conducted a research with the objective of diagnosis the financial performance analysis of Bishal Cooperative Society Ltd. in the framework of PEARLS with the help of secondary information using PEARLS tools[Prem Sharma, 2008]. The major finding from his study were able to allocate the allowance for loan losses, maintaining non-earning liquid investments up to its standard, lower the operating expenses consecutively over the periods, the institutional capital has not been attained up to its norms. This is due to the poor assets, which have been fallen in high delinquency and able to attract more deposits so as to augment the total assets. The poor in savings to invest in quality loan portfolio and delinquency has resulted sternly from earning or significant level with respect to PEARLS standard. the institution in the event of focusing primarily in savings deposits to invest in quality loan portfolio will substantially add up the institutional capital as a result of yielding earnings that shall eventually ensures the sound financial health of BCSL. He recommended that the institution to focus on the saving deposits as the main source of growth in total assets and develop an effective marketing program to attract more savings.

Pokhrel has conducted a research on the overall situation of the cooperative movement in Nepal [Binod Bihari Pokhrel, 1988]. According to his study, all most all of the village of 30 district were covered by Sajha Societies upto 1988 by which 43 percent cooperatives were suffering from loss in 1983/84. Out of those societies 41.20 percent were of Terai region and 58.80 percent were of hilly region. The same position seems to have been existed in the proceeding years. It shows that the Sajha of Hilly region were poorer than that of Terai. The study concludes that the problems are;

- Lack of cooperative education,
- Lack of fund
- Political interference and public apathy
- Lack of loyalty
- Lack of spontaneity towards cooperation

- Absence of lonely service
- Absence of good process of loan disbursement and payment.
- Lack of efficient management
- Lack of specific and stable policy and central level coordination

The study has suggested that remove the various problems of the cooperative movement of the country and for paying the due attention to the developmental activities and control the existing irregularities and weaknesses by establishing a sound accounting information system. The study commented that the major problems faced by the cooperative are lack of systematic, scientific complete and comprehensive system of collecting processing storing producing and communicating the accounting data and information. The concerned interested parties and general public does not properly identify such various problems of the cooperatives of our country yet.

CHAPTER THREE
RESEARCH METHODOLOGY

This chapter deals with the research design, justification for the selected study unit, nature and sources of data, data collection method, data processing and analysis, PEARLS financial tools and limitation of the methodology.

3.1 Research Design

The study of research design refers to the case study research design. It is of descriptive as well as analytical approaches to achieve the desired objectives. This study is an examination and evaluation of performance of Royal Cooperative Society Ltd. (RCSL) in the framework of PEARLS and traces out the basic practices of the institution. The quantitative method on this study will give rise to objective assessment based on the information and data.

3.2 Justification for the Selection of Study Unit

Despite, the RCSL is not formally registered institution in Nepal Rastra Bank, it has played a key role in terms of its services through an effective operation. It gives the services to the lower income community member through the saving and credit facilities. So, the role in its sound performance, the actual performance played therein is of necessary to find out the gap with the application of PEARLS framework. In addition to it, the data availability comes as a significant part, which other MFIs may not have according to PEARLS indicators. This study is an attempt to find out the deficiencies faced by the RCSL and taking this institution as a study unit through numerous indicators under PEARLS.

3.3 Nature and Sources of Data

The nature of data in this study is based on secondary data. Mainly, the data is collected from the annual reports, official reports and other relevant information of RCSL. Moreover, the information was also available from the different journals, articles, books and websites. Supplementary other information regarding the performance of the institution is collected by raising questions with senior level of employees of the institution.

3.4 Data Collection Method

The study is entirely base on the historical data disclosed by annual reports and official reports of RCSL. The annual reports, official reports and relevant information are collected from RCSL and other relevant information are collected from Department of Cooperative and District Cooperative Office, Kaski, Pokhara.

3.5 Data Processing and Analysis

Those data are processed with both manually and computerized after extracting the necessary data from annual and other relevant statements. These data is entered into the spreadsheet to work out the PEARLS financial ratios and prepare the necessary figures. Finally, the different financial tools under PEARLS are worked out with the help of computer programs.

3.6 PEARLS Financial Tools

3.6.1 Protection (P)

Adequate protection to the assets can make protection to the saving of the member-client in a cooperative. In this section protection considers provision of allowances for loan losses and solvency. Making provision of adequacy of allowances is a crucial role that safeguards the member savings. The indicators in this section measure the adequacy of the provisions for loan losses. Under protection, WOCCU inc. has developed six indicators: allowance for loan losses to allowances required for loans delinquent >12 months (P_1), net allowance for loan losses to allowances required for loans delinquent < 12 months (P_2), total charge off delinquent loans > 12 months (P_3), quarterly loan charges off to total loan portfolio (P_4), accumulated recovered charge off to accumulated charge off (P_5) and solvency (P_6). Only P_1, P_2 and P_6 are calculated in this study. Remaining indicators have not been calculated due to the data un-availability.

3.6.2 Effective Financial Structure (E)

Effective financial structure is necessary to achieve safety, soundness and profitability, while at the same time, positioning the MFI for aggressive real growth. The composition of debt and equity should be appropriate to ensure that the institution

has sound proportion of financial structure. The indicators in this section measure the composition of the most important account on the Balance Sheet.

PEARLS system measures MFI's assets, liabilities and capital and then recommends the ideal structure. MFIs are to regard seriously in productive assets to have a sound and stream of earnings that gives sustainability to the institution. Under Effective Financial Structure (E), WOCCU Inc. has developed nine indicators i.e. net loans to total assets (E_1), liquid investments to total assets (E_2), financial investments to total assets (E_3), non-financial investments to total assets (E_4), savings deposits to total assets (E_5), borrowed funds to total assets (E_6), member shares to total assets (E_7), institutional capital to total assets (E_8) and net institutional capital to total assets (E_9) in which E_1, E_2, E_5, E_7, and E_9 are calculated in this study. Remaining indicators have not been calculated due to the data un-availability.

3.6.3 Assets Quality (A)

Assets Quality measures the percentage of non-earning assets that negatively affect the profitability and solvency of the institution. The indicators are loan delinquency, non-earning assets and financing of non-earning assets. PEARLS indicators are used to identify the impact of non-earning assets by analyzing delinquency ratios, percentage of non-earning assets and financing of non-earning assets. Under Assets Quality (A), WOCCU Inc. has developed three indicators i.e. total loan delinquency to total loan portfolio (A_1), total non-earning assets to total assets (A_2) and net institutional capital + transitory capital + non-interest bearing liabilities to non-earning assets (A_3), in which A_1, A_2 acre calculated in this study. Remaining indicators have not been calculated due to the data un-availability.

3.6.4 Rate of Returns and Costs (R)

These indicators measure the average income yield of reach of the most productive assets of the Balance Sheet. In addition, they measure the average yield (cost) for each of the most important liability and capital accounts. The yields are actual investment returns and not the typical "spread analysis" yields that are figured on the basis of

average assets. The corresponding yields indicate whether the MFIs are earning and paying market rates on its assets, liabilities and capital.

PEARLS calculate yields on the basis of average outstanding investments, unlike other systems that calculate yields on the basis of average assets. Under rate of returns and costs (R), WOCCU Inc. has developed twelve indicators i.e. total loan income to average net loan portfolio (R_1), liquid investment income to average liquid investments (R_2), financial investment income to average financial investments (R_3), non-financial investment income to average non-financial investments (R_4), financial cost: savings deposits to average savings deposits (R_5), financial cost: borrowed funds to average borrowed funds (R_6), financial cost: member shares to average member shares (R_7), gross margin to average total assets (R_8), operating expenses to average total assets (R_9), provision for loan losses to average total assets (R_{10}), non-recurring income or expenses to average total assets (R_{11}) and net income to average total assets (R_{12}). R_1, R_2, R_5, R_7, R_8, R_9, R_{10}, and R_{12} are calculated in this study. Remaining indicators have not been calculated due to the data un-availability.

3.6.5 Liquidity (L)

Liquidity is necessary that institution should manage effectively to meet deposit withdrawal requests and liquidity reserve requirements. But excess idle cash also hinders profitability of institution. The institution should ensure that such provision of cash would not affect the profitability. Its indicators measure to ensure that the institution has appropriate cash to manage the deposit withdrawal and liquidity reserve requirements. In addition, the idle cash is also measured to ensure that this non-earning asset does not unduly affect profitability. PEARLS analyze liquidity from two perspectives: obligatory liquidity reserves and idle liquidity reserves. Under liquidity (L), WOCCU Inc. has developed three indicators i.e. liquid investments + liquid assets - short-term payables to savings deposits (L_1), liquidity reserves to savings deposits (L_2) and non-earning liquid assets to total assets (L_3). L_2 is calculated in this study.

3.6.6 Sign of Growth (S)

Growth of assets is necessary of any institutions for the sustainability. Despite, the growth of assets, profitability is of vital which determines the soundness of institutions. The diversification of loan, savings deposits and institutional capital greatly affect in the profitability of institutions. The indicators of this section measure the percentage of growth in each of the most important accounts on the financial statement, as well as growth in membership. In inflationary economics, real growth (after subtracting inflation) is a key to the long run viability of the CU. Under sign of growth (S), WOCCU Inc. has developed eleven indicators i.e. growth in loans (S_1), growth in liquid investments (S_2), growth in financial investments (S_3), growth in non-financial investments (S_4), growth in savings deposits (S_5), growth in borrowed funds (S_6), growth in member shares (S_7), growth in institutional capital (S_8), growth in net institutional capital (S_9), growth in membership (S_{10}) and growth in total assets (S11). S_1, S_2, S_5, S_7, S_8, S_{10} and S_{11} are calculated in this study. Remaining indicators have not been calculated due to the data un-availability. WOCCU Inc. has categorized two types of membership i.e. founder members and general members in MFIs. In accordance of Nepalese cooperative act 2048, it was found the single category, which is described as general members.

3.7 Limitation of the Methodology

This research study is carried out within the framework of case study research design, it is bounded by its own methodology. So, it can't be said that it is free from any limitation. The PEARLS tools have been applied as developed for CUs which is slightly, through developed for micro-finance institution, different in its working pattern. In addition to it, the different tools and working methodologies in different countries differ as they have their own norms and standard. So, the tools under PEARLS may not be appropriate in every aspect of this case study. The financial tools, which have been applied to analyze the collected data, are based on the CU's standards through its past experiences, which might have adhered with several assumptions. So, the reliability of the analysis depends upon the circumstances on which the tools are based.

CHAPTER FOUR
PRESENTATION AND ANALYSIS OF DATA

This chapter deals with the presentation and analysis of data collected from the different sources. As stated in the theoretical prescription, the financial performance analysis of RCSL is concentrated in the six components, PEARLS: Protection, Effective financial structure, Assets quality, Rates of returns and costs, Liquidity and Sign of growth. The data collected from different annual reports and office reports of RCSL have been analyzed with the application of PEARLS. The major findings thereby have been emanated as derived from analysis of data.

4.1 Data Presentation and Analysis

4.1.1 Protection (P)

Protection is measured by comparing the provision for loan losses beside the amount of delinquent loans. It is deemed adequate if an institution has sufficient provisions to cover 100 percent of all loans delinquent for more than 1 year. Institution should adequately provide for their loan losses as they frequently request the authority to charge off loans prior to the expiry of the period.

Generally, the loan receiver in prescribed time schedule should make protection against the loan loss that occurs due to un-repayment of principal loan amount. The provision for loan losses is a non-cash tax-deductible expenses that is used to defend to any credit risk that falls due to failure in the repayment of loan and interest. It is the current period's allocation to the allowance for loan losses listed on the balance sheet. This item represents the institution' prediction of loan at risk of default for the period.

As stated in research methods, only the tools P_1, P_2, and P_6 have been calculated and analyzed under protection. The relevant data related to write-off delinquency loan, annual and accumulated loan write-off and accumulated loan recoveries were not available to calculate and analyze.

4.1.1.1 Allowances for Loan Losses to Allowances Required for Loans Delinquent > 12 Months (P_1)

This ratio measures the adequacy of the allowances for loan losses while compared to the allowances required for covering all loans delinquent more than 12 months.

Table 4.1: Allowances for Loan Losses to Allowances Required for Loans Delinquent > 12 Months

(NRs. '000)

P_1	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total allowance for loan losses	17	53	137	250	359
b. Loan delinquency > 12 months	33	57	70	94	121
Allowances for loan losses/Delinquency > 12 months (%)	51.52	92.98	195.71	265.96	296.69
PEARLS Standard (%)	100	100	100	100	100

Source: **Annual Reports, RCSL**

The above data shows that the ratio of allowances for loan losses to allowances required for loans delinquent > 12 months are 51.52%, 92.98%, 195.71%, 265.96% and 296.69% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are fluctuating but in increasing trend. In FY 061/62 the ratio is fell down to 51.15%, which is lower than the PEARLS standard. It is because insufficient of allowance for losses rather than loan delinquency. But in other FYs, it is higher than the standard of PEARLS except FY 062/63, which is little bit lower. It shows that the management has adopted the good policy about the loan delinquency with respect to allowances for loan losses.

4.1.1.2 Net Allowance for Loan losses to Delinquency of 1-12 months (P_2)

This ratio measures the adequacy of the net allowances for loan losses while compared to the allowances required for covering all loans delinquent 1-12 months.

Table 4.2: Net Allowance for Loan losses to Delinquency of 1-12 months

(NRs. '000)

P_2	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Allowance for Loan losses	17	53	137	250	359
b. Loan Delinquency > 12 months	33	57	70	94	121
c. Loan Delinquency of 1-12 months	24	38	64	93	113
Net Allowances for Loan losses/Delinquency of 1-12 months (%)	(66.67)	(10.53)	104.69	167.74	210.62
PEARLS Standard (%)	35	35	35	35	35

Source: **Annual Reports, RCSL**

The above data shows that the ratio of net allowances for loan losses to allowances required for loans delinquent 1-12 months are (66.67)%, (10.53)%, 104..69%, 167.74% and 210.62% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are fluctuating but in increasing trend. In FYs 061/62 and 062/63 the ratios were negative, which were lower than the PEARLS standard. It is because insufficient of allowance for losses rather than loan delinquency. But in other FYs, the ratios are far above than the standard of PEARLS. It shows that the management has allocated insufficient of allowance for losses in first two FYs but in other FYs has allocated much sufficient of allowance for losses. Sufficient loan loss provision indicates that the institution has more strong in the institutional capital.

4.1.1.3 Net Value of Assets to Total Shares & Deposits (P_6)

This ratio measures the relative worth of one rupee in member-client savings after adjusting for known and probable loan losses. The net value of asset is calculated by deducting the total delinquency loans, liabilities and problem assets from the sum of total assets and allowances for loan loss provision and saving deposits.

Table 4.3: Net Value of Assets to Total Shares & Deposits

(NRs. '000)

P_6	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Net Value of Assets	7850	17124	21202	24256	40290
b. Total Shares and Deposits	7910	17232	21178	24199	40195
Net Value of Assets / Total Shares and Deposits (%)	99.24	99.37	100.11	100.24	100.23
PEARLS Standard (%)	≥ 100	≥ 100	≥ 100	≥ 100	≥ 100

Source: **Annual Reports, RCSL**

The above data shows that the ratio of net value of assets to total shares and deposits are 99.24%, 99.37%, 100.11%, 100.24% and 100.23% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. In every FY, the ratios are within the standard of PEARLS. It shows that the management has adopted the good policy about the solvency.

4.1.2 Effective Financial Structure (E)

Financial structure depicts on the effective management of sources and uses of funds of MFIs. It is the single most important in determining growth potential, earnings capacity and overall financial strength of the institution. MFIs are encouraged to maximize earning assets as the means to achieve sufficient earnings. As stated in research methodology, the tools E_1, E_2, E_5, E_7, E_8 and E_9 have been calculated and analyzed under the Effective Financial Structure. The relevant data related to financial, non-financial investment and external credit were not available to calculate and analyze the E_3, E_4 and E_6.

4.1.2.1 Net Loans to Total Assets (E_1)

This ratio measures the percentage of total assets invested in the loan portfolio. The net loan is loan after the deduction of total allowance for loan losses from the gross loan portfolio of the institution. According to CU model, setting different interest rates on loans with respect to its purpose, amounts and terms and condition is of crucial need that institutions should strongly stand for. The income to institution is largely dependent upon the level of loans transaction and its quality. In the case of delinquency level, the institution has to allocate the adequate allowances for loan losses.

Table 4.4: Net Loans to Total Assets

(NRs. '000)

E_1	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Gross loan Portfolio outstanding	8277	9451	19553	27404	46257
b. Total Allowance for Loan losses	17	53	137	250	359
c. Total Assets	9743	17657	24258	31955	57177
Net Loans /Total Assets (%)	84.78	53.23	80.04	84.98	80.27
PEARLS Standard (%)	70-80	70-80	70-80	70-80	70-80

Source: **Annual Reports, RCSL**

The above data shows that the ratio of net loans to total assets are 84.78%, 53.23%, 80.04%, 84.98% and 80.27% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. In 062/63 the ratio is fell down to 53.23%. But in other FYs, it is little bit higher than the standard of PEARLS. It shows that, in an average, the ratios are in PEARLS standard except FY 062/63.

4.1.2.2 Liquid Investment to Total Assets (E_2)

It measures the percentage of total assets invested in short-term investments. Excess liquidity is discouraged because the margins on liquid investments are significantly lower than those earned on the loan portfolio. In the event of high investments in this category, it invariably affects the gross spread and indirectly affects the loan portfolio and the institutional capital. The level of investments in short-term should be in relation to member's withdrawal.

Table 4.5: **Liquid Investment to Total Assets**

(NRs. '000)

E_2	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Liquid Investments	585	5511	2625	2785	8957
b. Total Assets	9743	17657	24258	31955	57177
Total Liquid Investment /Total Assets (%)	6.00	31.21	10.82	8.72	15.67
PEARLS Standard (%)	Max 20	Max 20	Max 20	Max 20	Max 20

Source: **Annual Reports, RCSL**

The above data shows that the ratio of liquid investment to total assets are 6.00%, 31.21%, 10.82%, 8.72% and 15.67% in FY 061/62, 062/63, 063/64, 064/65 and

065/66 respectively. In 062/63 the ratio 31.21 is higher the PEARLS standard. But in other FYs, the ratio is standard of PEARLS in fluctuating trend. It shows that the ratio is in PEARLS standard except FY 062/63.

4.1.2.3 Saving Deposit to Total Assets (E_5)

It measures the percentage of total assets financed by savings deposits. The heavy deposit savings indicate that the institution has developed effective marketing programs and achieved financial independence. Saving deposit is affected by the interest rates of the institution offers to the depositors. According to CU model, setting saving rates within the market average is a mandatory. But, attempting to pay more than the market rate may hinder a problem. Such interest charges should be below the loans rates charged.

Table 4.6: Saving Deposits to Total Assets

(NRs. '000)

E_5	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Saving Deposits	9160	19396	25476	32944	60085
b. Total Assets	9743	17657	24258	31955	57177
Total Saving Deposits /Total Assets (%)	73.49	81.52	83.39	84.36	84.80
PEARLS Standard (%)	70-80	70-80	70-80	70-80	70-80

Source: **Annual Reports, RCSL**

The above data shows that the ratio of saving deposits to total assets are 73.49%, 81.52%, 83.39%, 84.36% and 84.80% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. In 061/62 the ratio 73.49% is quite in PEARLS standard. But in other FYs, the ratio is little bit higher than that of PEARLS standard. It shows that in an average the ratio is in PEARLS standard.

4.1.2.4 Member Share Capital to Total Assets (E_7)

It measures the percentage of total assets financed by member share capital. The more share capital indicates that the institution has strong with its paid-up capital.

Table 4.7: Member Share Capital to Total Assets

(NRs. '000)

E_7	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Member Share Capital	1798	1879	2158	3178	2985
b. Total Assets	9743	17657	24258	31955	57177
Member Share Capital /Total Assets (%)	18.24	10.38	9.32	9.28	5.25
PEARLS Standard (%)	10-20	10-20	10-20	10-20	10-20

Source: **Annual Reports, BCSL**

The above data shows that the ratio of member share capital to total assets are 18.24%, 10.38%, 9.32%, 9.28% and 5.25% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratio is fluctuating but in decreasing trend. In FY 061/62 and 062/63 the ratio is quite in PEARLS standard. But in FY 063/64 and 064/65 the ratio is little bit lower than that of PEARLS standard. It shows that in an average the ratio is in PEARLS standard except FY 065/66.

4.1.2.4 Institutional Capital to Total Assets (E_9)

It measures the percentage of total assets financed by institutional capital. Since institutional capital has no explicit interest cost, it will generate 100 percent return to the institutions investing to the productive assets. According to CU, focus on epidemic is a crucial that institution should pay observe in its operation. Institution need to strengthen its institutional capital so that it can withstand losses associated with epidemic.

Table 4.7: Institutional Capital to Total Assets

(NRs. '000)

E_9	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Institutional Capital	104	198	398	593	865
b. Total Assets	9743	17657	24258	31955	57177
Institutional Capital /Total Assets (%)	1.07	1.12	1.64	1.86	1.51
PEARLS Standard (%)	Min 10	Min 10	Min 10	Min 10	Min 10

Source: **Annual Reports, RCSL**

The above data shows that the ratio of institutional capital to total assets are 1.07%, 1.12%, 1.64%, 1.86% and 1.51% in FY 061/62, 062/63, 063/64, 064/65 and 065/66

respectively. The ratio is far below the PEARLS standard. This occurred that the institution could not allocate sufficient capital due to failure in earnings.

4.1.3 Assets Quality (A)

Asset Quality indicators measure the impact of assets which do not generate income such as loan delinquency and non-earning assets. The delinquency ratio is the most important measurement of institutional weakness. Delinquency is measured using the portfolio at risk method, which defines as delinquent the entire outstanding balance of any loan affected by amount overdue. The higher ratio of non-earning assets indicate the more difficult to generate sufficient earnings.

4.1.3.1 Total Loan Delinquency to Total Loan Portfolio (A_1)

It measures the total percentage of delinquency in the loan portfolio, using the criterion of outstanding delinquent loan balances instead of accumulated delinquent loan payments. The poor credit analysis put the institution into a serious problem in collection of loans on timely fashion. The institution in the event of the loan delinquency should surcharge of certain percent a month to mitigate the problem that might arise in its operation.

Table 4.10: Total Loan Delinquency to Total Loan Portfolio

(NRs. '000)

A_1	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Loan Delinquency	61	91	107	156	213
b. Total Loan Portfolio	9070	11118	17964	25548	41025
Total Loan Delinquency /Total Loan Portfolio (%)	0.67	0.82	0.59	0.62	0.51
PEARLS Standard (%)	≤ 5	≤ 5	≤ 5	≤ 5	≤ 5

Source: **Annual Reports, RCSL**

The above data shows that the ratio of total loan delinquency to total loan portfolio are 0.67%, 0.82%, 0.59%, 0.62% and 0.51% in FY 061/62, 062/63, 063/64, 064/65and 065/66 respectively. The ratios are within the PEARLS standard. In FY 062/63 the ratio is slightly higher to 0.82% than other FYs. It shows that the management has adopted the good policy about the loan delinquency.

4.1.3.2 Non-earning Assets to Total Assets (A_2)

It measures the percentage of the total assets, which do not produce income. Monitoring the ratio of non-earning assets to total assets comes at hand and ensured that savings deposits or member shares do not finance these non-earning assets. The non-earning assets include cash, fixed assets, advance, dues and other assets.

Table 4.11: Non-earning Assets to Total Assets

(NRs. '000)

A_2	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Non-earning Assets	584	1312	1415	1798	2189
b. Total Assets	9743	17657	24258	31955	57177
Non-earning Assets / Total Assets (%)	6.00	7.43	5.83	5.63	3.83
PEARLS Standard (%)	≤ 5	≤ 5	≤ 5	≤ 5	≤ 5

Source: **Annual Reports, RCSL**

The above data shows that the ratio of non-earning assets to total assets are 6.00%, 7.43%, 5.83%, 5.63% and 3.83% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratio is fluctuating but in decreasing trend. In FY 064/65 the ratio is quite in PEARLS standard. But in other FYs the ratio is little bit higher than that of PEARLS standard. It shows that the institution has high amount of non-earning assets.

4.1.4 Rate of Return and Cost (R)

Earning and costs are determined by dividing all interest income, delinquent interest penalties and commission from lending operations by the total loan portfolio to give the return on loans. This is compared to the return on financial investments, income from bank savings accounts and liquidity reserves divided by the amounts invested in those areas. This indicator measures the average income yield for each of the most productive assets. In addition, they measure the average yield for each of the most important liability and capital account. The indicators of return and costs monitor the return earned on each type of assets and costs on each type of liabilities. Under rate of returns and costs, the tools R_1, R_2, R_5, R_7, R_8, R_9, R_{10}, R_{11} and R_{12} have been calculated and analyzed. The relevant data related to financial, non-financial income and external credit were not available to calculate and analyze the R_3, R_4 and R_6.

4.1.4.1 Net Loan Income to Average Loan Portfolio (R_1)

It measures the yield on the loan portfolio during last year. The purpose of this ratio is the loan prices to be set at entrepreneurial rates. The entrepreneurial rate needs to cover the cost of funds, the cost of operations and administration, the cost of provisions and the cost of contributions to increase capital at least 10 percent. The loan income also includes commissions, fees and delinquent interest penalties. When institution falls in a high loan delinquency, it encounters a problem in earning that cover all the costs. This ratio is most affected by P_1 and P_2.

Table 4.13: Net Loan Income to Average Loan Portfolio

(NRs. '000)

R_1	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Net Loan Income	2427	2915	4673	6110	8388
b. Net Loan Portfolio as of Current year-end	10254	12391	24411	34148	55680
c. Net Loan Portfolio as of Last year-end	7185	10254	12391	24411	34148
Net Loan Income /Avg. Net Loan Portfolio (%)	27.83	25.75	25.40	20.87	18.68

Source: **Annual Reports, RCSL**

The above data shows that the ratio of net loan income to average loan portfolio are 27.83%, 25.75%, 25.40%, 20.87% and 18.68% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are seemed quite high but in decreasing trend in the study period. This ratio should be greater than the entrepreneurial rate. It is satisfactory, as it has covered the cost of funds, cost of administration and operation, cost of provisions and the cost of contribution to increase capital. The institution has not, however, attained the goal of institutional capital to be at least 10 percent.

4.1.4.2 Total Liquid Investment Income to Average Liquid Investment (R_2)

It measures the yield on short-term investments i.e. cash at bank which gives such interest yield in the institution. This ratio depends upon market rate.

Table 4.14: Total Liquid Investment Income to Average Liquid Investment

(NRs. '000)

R_2	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Liquid Investment Income	23	103	111	48	256
b. Liquid Investment as of Current year-end	685	8592	3619	3014	10373
c. Liquid Investment as of Last year-end	498	685	8592	3619	3014
Total Liquid Investment Income / Avg. Liquid Investment (%)	3.89	2.22	1.82	1.45	3.82

Source: **Annual Reports, RCSL**

The above data shows that the ratio of total liquid investment income to average liquid investment are 3.89%, 2.22%, 1.82%, 1.45% and 3.82% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. In FY 061/62 the ratio is 3.89 percent then decreased up to FY 064/65 to 1.45 percent and then increased to 3.82 percent in FY 065/66. The ratios are seemed quite low during the study period. This ratio is dependent upon the market rate.

4.1.4.3 Total Interest Cost on Saving Deposits to Average Saving Deposits (R_5)

It measures the yield (cost) of saving deposits. The total interest and premium paid on saving deposits and taxes paid by MFI on saving deposits interest are included in the yield (cost). This ratio is most affected by the quality of assets and the overall income generated by the institutions. Quality assets yield high earnings. Most of the times, institutions can offer a competitive interest rate to the deposits in the financial market.

Table 4.15: Total Interest Cost on Saving Deposits to Average Saving Deposits

(NRs. '000)

R_5	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Interest Paid on Saving Deposits	787	1475	2351	3458	5351
b. Total Saving Deposits as of Current year-end	9160	19396	25476	32944	60085
c. Total Saving Deposits as of Last year-end	6066	9160	19396	25476	32944
Total Interest Paid on Saving Deposits/ Avg. Saving Deposits (%)	10.34	10.33	10.48	11.84	11.50

Source: **Annual Reports, RCSL**

The above data shows that the ratio of interest cost of saving deposits to total saving deposits are 10.34%, 10.33%, 10.48%, 11.84% and 11.50% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The PEARLS standard suggests maintaining the market rate above inflation rate so as to increase the savings of member-client. Market rates stood above the inflation rates throughout the study period.

4.1.4.4 Total Interest (Dividend) Cost on Shares to Average Member Shares (R_7)

It measures the yield (cost) of member shares. The total dividend and premium paid on shares are included in the yield (cost). This ratio is most affected by the quality of assets and the overall income generated by the institutions. Quality assets yield high earnings. Most of the times, institutions can offer a competitive dividend rate to the member shares in the financial market.

Table 4.16: Total Dividend Cost on Shares to Average Member Shares

(NRs. '000)

R_7	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Interest (Dividend) Paid on Shares	61	115	274	370	370
b. Total Member Shares as of Current year-end	2047	2293	2737	3527	3521
c. Total Member Shares as of Last year-end	1153	2047	2293	2737	3527
Total Interest (Dividend) Paid on Shares / Avg. Member Shares (%)	3.81	5.30	10.89	11.81	10.50
PEARLS Standard (%)	≥ R5	≥ R5	≥ R5	≥ R5	≥ R5

Source: **Annual Reports, RCSL**

The above data shows that the ratio of interest (dividend) cost on shares to average member shares are 3.81%, 5.30%, 10.89%, 11.81% and 11.50% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The PEARLS standard suggests that maintaining the dividend ratio greater than or equal to interest cost ratio of the institution. Here, in FYs 061/62 and 062/63, the ratio seemed too lower. But, in FYs 063/64, 064/65 and 065/66 the institution able to ensure the dividend ratio within the PEARLS standard.

4.1.4.5 Total Gross Margin to Average Total Assets (R_8)

It measures the gross income margin generated, expressed as yield on all assets before subtracting operating expenses, provisions for loan losses and other extraordinary items. This indicator provides the institutions in yield of an adequate income to cover all operating expenses and allowances for loan losses and provide for adequate increases in institutional capital. This ratio is linked to R_9, R_{11} and R_{12}. It is affected by income from loan, level of delinquency loan, non-earning assets, liquidity and the financial costs. Adequate support of liquidity, a higher delinquency loans, non-earning assets and heavy incurrence of financial costs hold back the earnings, which determine the sustainability of institution. Minimizing the operating expenses and augmenting the earning level from both recurring and non-recurring activities significantly give rise to increase this ratio.

Table 4.17: Total Gross Margin to Average Total Assets

(NRs. '000)

R_8	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Gross Margin	1618	1529	2303	2334	3085
b. Total Assets as of Current year-end	9743	17657	24258	31955	57177
c. Total Assets as of Last year-end	8948	11743	22657	30058	39955
Total Gross Margin / Avg. Total Assets (%)	17.31	10.40	9.82	7.53	6.35

Source: **Annual Reports, RCSL**

The above data shows that the ratio of gross margin to average total assets are 17.31%, 10.40%, 9.82%, 7.53% and 6.35% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratio is fluctuating but in decreasing trend. This ratio is linked with R_9, R_{11} and R_{12}. The institution has not been able to get lower R_9, however R_{11} is minimal but R_{12} is not sound to ensure this ratio within the PEARLS standard.

4.1.4.6 Total Operating Expenses to Average Total Assets (R_9)

It measures the cost associated with the management of institution overall assets. This cost is measured as a percentage of total assets and indicates the degree of operational efficiency or inefficiency. These costs include the both office management cost and staff salary. For survival of institution, a careful review in administrative structure is

dire to determine the need for each position and to readjust salaries. Operating expenses should not be incurred over the allocation of budget. Most of the times, institutions do not use budget as a tool for the authorization of expenses. A sound resource only ensures the institution that it can spend but with a thorough analysis in the allocation of resources for expenses.

Table 4.18: Total Operating Expenses to Average Total Assets

(NRs. '000)

R_9	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Operating Expenses	1528	1351	1831	1765	2470
b. Total Assets as of Current year-end	9743	17657	24258	31955	57177
c. Total Assets as of Last year-end	8948	11743	22657	30058	39955
Total Operating Expenses / Avg. Total Assets (%)	16.35	9.19	7.80	5.69	5.08
PEARLS Standard (%)	5	5	5	5	5

Source: **Annual Reports, RCSL**

The above data shows that the ratio of operating to average total assets are 16.35%, 9.19%, 7.80%, 5.69% and 5.08% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratio is fluctuating but in decreasing trend. In FY 061/62, the ratio is very high but in FYs 062/63 and 063/64 the ratio is slightly higher than the PEARLS standard. The later FYs 064/65 and 065/66 the institution has maintained the ratio in average with PEARLS standard. It shows that management is increasing its efficiency in controlling the operating expenses during the study period.

4.1.4.7 Provision for Loan Losses to Average Total Assets (R_{10})

It measures the cost of losses from risk assets such as delinquent loans or un-collectible accounts receivables. This cost is differing form other operational expenses and should be separated to highlight the effectiveness of MFI collection policies and procedures. PEARLS suggests the institution to maintain the provision enough to cover 100 percent of delinquent loans for more than 12 months and 35 percent for loans delinquent from 1 to 12 months. Generally, lowering the delinquency as much as it can gives a safe cushion to institution form going into an adverse effect.

Table 4.19: Provision for Loan Losses to Average Total Assets

(NRs. '000)

R_{10}	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Loan loss Provision	17	53	137	250	359
b. Total Assets as of Current year-end	9743	17657	24258	31955	57177
c. Total Assets as of Last year-end	7945	9743	17657	24258	31955
Total Loan loss Provision / Avg. Total Assets (%)	0.24	0.41	0.61	0.83	0.76

Source: **Annual Reports, RCSL**

The above data shows that the ratio of provision for loan losses to average total assets are 0.24%, 0.41%, 0.61%, 0.83% and 0.76% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratio is increasing up to 0.83% in FY 064/65 then it is decreased to 0.76% in FY 065/66. This ratio depends upon the level of loan delinquencies. It shows that institution has maintained these ratios in terms of loan delinquency.

4.1.4.9 Net Income to Average Total Assets (R_{12})

It measures the adequacy of earning and also the capacity to make institutional capital. This ratio is linked to R_9. Control and reduction of unnecessary overhead gets high earnings. Besides, a prompt collection of loan in the stipulated time frame produces the earnings. The high level delinquencies prohibit from earning the income. Such loans should be lowered and reinvested them in productive assets that give a good margin.

Table 4.20: Net Income to Average Total Assets

(NRs. '000)

R_{12}	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Net Income	119	254	546	761	747
b. Total Assets as of Current year-end	9743	17657	24258	31955	57177
c. Total Assets as of Last year-end	7945	9743	17657	24258	31955
Net Income / Avg. Total Assets (%)	1.27	1.73	2.33	2.45	1.54

Source: **Annual Reports, RCSL**

The above data shows that the ratio of net income to average total assets are 1.27%, 1.73%, 2.33%, 2.45% and 1.547% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratio, at inception, increased to 2.45% in the FY 064/65 from 1.27% in FY 061/62. It is in increasing trend up to FY 064/65, later, it decreased to 1.54% in FY 065/66. This ratio is linked to net institutional capital to total assets ratio, E_9. Since E_9 has not maintained its standard, the net income to total assets ratio is not adequate.

4.1.5 Liquidity (L)

Liquidity indicators measures if an institution is administering its cash to meet deposit withdrawal requests and liquidity reserve requirements while, at the same time minimizing the amount of idle funds that earn no interest income. Depositors' confidence will be destroyed if an institution is not able to serve client withdrawals. The "ideal" target is to maintain a minimum 20 percent of deposit savings in liquid accounts, after paying all immediate obligations less than 30 days. The idle liquid funds ratio should be as close to zero percent as possible. Under liquidity, the tools L_2 and L_3 have been calculated and analyzed.

4.1.5.1 Liquidity Reserve to Total Saving Deposits (L_2)

It measures the compliance with obligatory of CU or other liquidity reserve deposit requirements. An excess support of liquidity reserves encumbers institution from generating income. As the interest margin on depository institutions or other commercial banks is significantly low than investing them in productive assets, such deposition in liquidity reserves is discouraged to institutions. The heavy portion of liquidity leads to institution negativity in earning and institution needs to assess the level of liquidity to maintain to offset the unexpected demand from member's saving accounts.

Table 4.21: Liquidity Reserve to Total Saving Deposits

(NRs. '000)

L_2	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Earning Liquid Reserve	685	8592	3619	3014	10373
b. Total Non-earning Liquid Reserve	293	806	450	918	1083
c. Total Saving Deposits	9160	19396	25476	32944	60085
Liquid Reserve / Total Saving Deposits (%)	10.68	48.45	15.97	11.94	19.07
PEARLS Standard (%)	10	10	10	10	10

Source: **Annual Reports, RCSL**

The above data shows that the ratio of liquid reserve to total saving deposits are 10.68%, 48.45%, 15.97%, 11.94% and 19.07% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are fluctuating in decreasing trend. In FY 061/62, it meets the PEARLS standard. In FY 062/63, the ratio is very high then it is decreasing. In FY 064/65, the ratio is slightly higher to 11.94% and in the FY 063/64 and 065/66 the ratio is higher than the PEARLS standard.

4.1.6 Sign of Growth (S)

Growth is measured by inflation-adjusted real growth, which is the key to long-term viability. By comparing the growth in total assets to other key areas, it is possible to detect changes in the balance sheet structure, which have an impact on earnings. The loan portfolio is the most important and profitable institution's asset. The growth of total assets depends on the growth of savings. Growth of institutional capital, which consists almost entirely of retained surpluses, is the best indicator of profitability within the MFIs. One sign of success for a MFI is sustained growth of institutional capital, usually faster than the growth of total assets. PEARLS, the indicators measure both financial and membership growth. Under sign of growth, the indicators enables balance sheet account comparisons between structure and yield, while simultaneously trying to achieve real growth. Under sign of growth, the tools S_1, S_2, S_5, S_7, S_8, S_9, S_{10} and S_{11} have been calculated and analyzed.

4.1.6.1 Growth in Gross Loan (S_1)

It measures the growth of loan portfolio year-to-date. The likelihood of profitability is possible if growth in total loans keeps pace with growth in total assets. It is important

to know various investment opportunities for income. Loan portfolio is profitable for institution and emphasis should be set in such areas. The earning from loans and the provision of allowances for loan delinquency greatly affect in the growth in loans. A prompt collection of loan in a specified time schedule helps institution from falling in bracket of loan delinquency. When delinquencies do not occur, the earning of institution increases and can further be re-invested in productive assets, which yields income. This ratio is affected by R_1 and R_{10}. According to PEARLS standard, if institution needs to increase the percentage of total loans outstanding (E_1), the growth in loans (S_1) should be greater than growth in total assets (S_{11}).

Table 4.22: Growth in Loans

(NRs. '000)

S_1	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Gross Loan Portfolio as of Current year-end	6789	9857	19553	32168	41048
b. Gross Loan Portfolio as of Last year-end	4765	6789	9857	24553	25468
Growth in Gross Loan (%)	42.47	45.19	98.37	31.01	61.17

Source: **Annual Reports, RCSL**

The above data shows that the growth in gross loans are 42.47%, 5.19%, 98.37%, 31.01% and 61.17% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are in fluctuating trend during the study period. This growth is dependant with E_1. Since the net loan is in tune with the total assets the growth in loans is satisfactory.

4.1.6.2 Growth in Liquid Investment (S_2)

It measures the growth of liquid investment year-to-date. Generally, excess investments in the liquid assets are discouraged due to its low earning. A heavy investment in liquid assets impeded the institution from investing in productive assets. According to PEARLS standard, if institution needs to increase the percentage of total loans outstanding (E_2), the growth in loans (S_2) should be greater than growth in total assets (S_{11}).

Table 4.25: Growth in Liquid Investment

(NRs. '000)

S_2	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Liquid Investment as of Current year-end	685	8592	3619	3014	10373
b. Liquid Investment as of Last year-end	498	685	8592	3619	3014
Growth in Liquid Investment (%)	37.55	1154.31	(57.88)	(16.72)	244.16

Source: **Annual Reports, RCSL**

The above data shows that the growth in liquid investments are 37.55%, 1154.31%, (57.88)%, (16.72)% and 244.16% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are in fluctuating trend during the study period. In FY 062/63, the ratio is extremely high which is 1154.31 percent then declining following two years and grow up in FY 065/66 to 244.16 percent. This growth is dependant with E_2. Since the liquid investment is in tune with the total assets the growth in liquid investments is satisfactory.

4.1.6.3 Growth in Saving Deposits (S_5)

It measures the year-to-date growth of savings deposits. Saving deposits are the cornerstones of institution growth. Its growth largely governs the change in total assets if mobilized properly. The growth of total assets is dependent on the growth of savings. The skill in marketing program will help in accumulating the saving deposits, which affect growth in other key areas. The growth is dependent on E_5.

Table 4.26: Growth in Saving Deposits

(NRs. '000)

S_5	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Saving Deposits as of Current year-end	9160	19396	25476	32944	60085
b. Total Saving Deposits as of Last year-end	6066	9160	19396	25476	32944
Growth in Saving Deposits (%)	51.01	111.75	31.35	29.31	82.39

Source: **Annual Reports, RCSL**

The above data shows that the growth in saving deposits are 51.01%, 111.75%, 31.35%, 29.31% and 82.39% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are in fluctuating trend during the study period. In FY 062/63,

the ratio is increased to 111.75 percent from 51.01 percent in FY 061/62 then it is going to decreased the following two years. In FY 065/66 it is increased to 82.39 percent. This growth is dependant with E_5. Since the saving deposits to total assets are about within in the range, the growth in saving deposits is also satisfactory with in standard.

4.1.6.4 Growth in Members Share Capital (S_7)

It measures the year-to-date growth of members share capital. The growth of member shares is dependent on the growth of institutional earning. High earning indicates the high dividend pay out ratio and vice versa.

Table 4.28: Growth in Members Share Capital

(NRs. '000)

S_7	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Member Share as of Current year-end	2047	2293	2737	3527	3521
b. Total Member Share as of Last year-end	1153	2047	2293	2737	3527
Growth in Member share (%)	77.54	12.02	19.36	28.86	(0.17)

Source: **Annual Reports, RCSL**

The above data shows that the growth in member shares are 77.54%, 12.02%, 19.36%, 28.86% and (0.17)% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are in fluctuating trend during the study period. In FY 065/66, the ratio is in negative to 0.17 percent. It shows that the shareholders returned the paid-up capital. In other FYs it seems satisfactory. This growth is dependant with E_7. Since the member share capital to total assets are about within in the range except FY 065/66, the growth in saving deposits is also satisfactory with in standard.

4.1.6.5 Growth in Institutional Capital (S_8)

It measures the growth of institutional capital year-to-date. Usually, growth in institutional capital should be greater than the growth of total assets. Static or declining growth tends in institutional capital usually indicates a problem with earnings. Earnings are necessary of a strong institutional reserve. Institutional capital reserve is of essential and it should be added to get earnings. The problem may arise

in the addition of institutional capital reserves if earnings are low. The growth is dependent on E_8.

Table 4.29: Growth in Institutional Capital

(NRs. '000)

S_8	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Institutional Capital as of Current year-end	125	269	581	893	1065
b. Total Institutional Capital as of Last year-end	28	125	269	581	893
Growth in Institutional Capital (%)	346.43	115.20	115.99	53.70	19.26

Source: **Annual Reports, RCSL**

The above data shows that the growth in institutional capital is 346.43%, 115.20%, 115.19%, 53.70% and 19.26% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are fluctuating but in decreasing trend during the study period. In FY 061/62, the ratio is very high which is to 346.43 percent. In FYs 062/63 and 063/64 it seems to decreasing but static range but in other following two FYs, the ratio is decreased one by one. This growth is dependant with E_8. Since the institutional capital to total assets is far below the standard, the growth in institutional capital is partially satisfactory with relation to E_8.

4.1.6.7 Growth in General Member (S_{10})

It measures the growth of general members year-to-date. Usually, membership growth ratio shows the trend of increasing or decreasing number of general members in the prescribed rules and regulations of the institution in terms of membership.

Table 4.30: Growth in Membership

S_{10}	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total General Member as of Current year-end	302	417	526	637	730
b. Total General Member as of Last year-end	195	302	417	526	637
Growth in Membership (%)	54.87	38.08	26.14	21.10	14.60
PEARLS Standard (%)	>12	>12	>12	>12	>12

Source: **Annual Reports, RCSL**

The above data shows that the growth in membership is 54.87%, 38.08%, 26.14%, 21.10% and 14.60% in FY FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are in decreasing trend during the study period. In FY 061/62, the ratio is higher which is to 54.87 percent and FY 065/66 it is decreased to 14.60 percent. The ratios are within the PEARLS standard but in decreasing year-to-date.

4.1.6.8 Growth in Total Assets (S_{11})

It measures the year-to-date growth of total assets. Total assets growth is one of the most important ratios. Strong and consistent growth in total assets improve many of the PEARLS ratios. By comparing the growth in total assets to other key areas, it is possible to detect changes in the balance sheet structure, which could have a positive or negative impact on earnings.

Table 4.31: Growth in Total Assets

(NRs. '000)

S_{11}	Fiscal Year				
	061/62	062/63	063/64	064/65	065/66
a. Total Assets as of Current year-end	9743	17657	24258	31955	57177
b. Total Assets as of Last year-end	7945	9743	17657	24258	31955
Growth in Total Assets (%)	22.63	81.23	37.38	31.73	78.93
Inflation	4.80	4.00	4.50	7.90	6.60

Source: **Annual Reports, RCSL**

The above data shows that the growth in total assets are 22.63%, 81.23%, 37.38%, 31.73% and 78.93% in FY 061/62, 062/63, 063/64, 064/65 and 065/66 respectively. The ratios are fluctuating during the study period. This ratio is dependant upon inflation rate. The growth of total assets ratio in all FYs is exceeded than the inflation rate. It shows that institution's assets growth rate has satisfactory in study period.

4.2 Major Findings of the Study

4.2.1 Over the five-year studies period, RCSL has been able to make provisions for delinquent loans at 100 percent in FYs 063/64 to 065/66. In FY 062/63 it is 92.98 percent, which is slightly lower and the FY 061/62 it is 51.52 percent, which is lower than PEARLS standard. The delinquency of institution in following three years is very high; it can defend with future uncertainties by the provision of allowances for the delinquency.

4.2.2 The ratio of net allowance for loan losses to delinquency of RCSL is negative in first two study periods and next three years is very high, which indicate that allocation of allowances of loan losses is inconsistent with loan delinquency. In the following three FYs, allowances of loan losses are very high rather than loan delinquency.

4.2.3 Over the five-year studies period, RCSL has been consistently maintained the solvency ratio, which the PEARLS standard is greater than or equal to 100 percent.

4.2.4 RCSL has consistently maintained the ratio of net loans to total assets around 80 percent and slightly above except FY 062/63. In FY 062/63, it was 53.23 percent, which is lower than the PEARLS standard (70-80 percent).

4.2.5 The ratio of liquid investment to total assets of RCSL over the five studies period is in near about the PEARLS standard except FY 062/63. In this FY, RCSL has the high amount of liquid assets (cash at bank), which shows high liquidity position of the institution.

4.2.6 RCSL has consistently maintained the ratio of saving deposits to total assets around 80 percent and slightly above, which is near about the PEARLS standard (70-80 percent).

4.2.7 The ratio of member share capital to total assets of RCSL over the five studies period is in near about the PEARLS standard except FY 064/65. In this FY, it is 5.25 percent, which is lower than the PEARLS standard (10-20 percent). In FYs 063/64 and 064/65 it is 9.32 and 9.28 percent, which is near about the PEARLS standard.

4.2.8 RCSL has not maintained the ratio of institutional capital to total assets within the PEARLS standard (min. 10 percent). The highest ratio of institution is 1.86 percent in FY 064/65 and the lowest is 1.07 percent in FY 061/62. The failure in the maintained of this ratio is inability of generating adequate earnings.

4.2.9 RCSL has maintained the ratio of total loan delinquency to total loan portfolio with the PEARLS standard (less than or equal to 5 percent). The highest ratio of institution is 0.82 percent in FY 062/63 and the lowest is 0.51 percent in FY 065/66.

4.2.10 For FY 065/66, RCSL has maintained the ratio of non-earning assets to total assets i.e. 3.83 percent, which is within PEARLS standard (less than or equal to 5 percent). In other FYs, the ratio has been above the PEARLS standard. The highest ratio was 7.43 percent in FY 062/63. This was due to high cash amount and increase in the acquisition of fixed assets.

4.2.11 Over the five year studies period, RCSL has managed to maintained net loan income to average loan portfolio ratio to cover the cost of funds, cost of administration and operation, the cost of provisions and the cost of contribution. These costs of contribution have satisfactorily added to increase institutional capital. The highest ratio of institution is 27.83 percent in FY 061/62 and the lowest is 18.68 percent in FY 065/66. This ratio is in decreasing trend in the consecutive years.

4.2.12 RCSL has experienced the liquid investment income to average liquid investment ratio is in fluctuating trend over the five years period. The highest ratio is 3.89 percent in FY 061/62 and the lowest is 1.45 percent in FY 064/65.

4.2.13 Over the five year studies period, RCSL has experienced the interest cost on saving deposits to average saving deposits (market rate) is above inflation rates. The highest ratio is 11.84 percent in FY 064/65 and the lowest is 10.33 percent in FY 062/63.

4.2.14 RCSL has experienced the dividend paid on shares to average member shares over the three consequences FYs 063/64 to 065/66 is in PEARLS standard

(greater than or equal to R_5). In the first two FYs, 061/62 and 062/63 the ratio was below the standard, which were 3.81 and 5.30 percent respectively.

4.2.15 The gross margin to average total assets ratio is consequently decreasing trend over the five year study periods. The highest ratio is 17.31 percent in FY 061/62 and the lowest is 6.35 percent in FY 065/66. The gross spread is not significantly increasing due to the assets quality. This spread should necessarily provide a cushion to boost-up the institutional capital up to its standard.

4.2.16 Over the first four fiscal year, RCSL has not able to maintained the ratio of operating expenses to average total assets. But in FY 065/66 it has maintained (slidely greater than 5) the ratio 5.08 percent within the PEARLS standard (5 percent). The highest ratio is 16.35 percent in FY 061/62 and the lowest is 5.08 percent in FY 065/66. This ratio is in decreasing trend in the consecutive years.

4.2.17 The loan loss provision to average total assets ratio is consequently increasing trend up to first four year study periods, then it was decreased to 0.76 percent in FY 065/66 from 0.83 percent in FY 064/65.

4.2.18 Over the five year studies period, RCSL has been able to maintain the ratio of net income to average total assets in terms of E_9. But it is not adequate in terms of growth of total assets. The highest ratio is 2.45 percent in FY 064/65 and the lowest is 1.27 percent in FY 061/62.

4.2.19 RCSL has been partially able to maintain the ratio of liquidity reserves to total saving deposits within the PEARLS standard of 10 percent over the five years study period. In FY 062/63 it was very high but in FY 063/64 and 065/66 it was little bit higher, which affects the earning power of institution.

4.2.20 RCSL has experienced the growth of loans fluctuating over the five-year study periods. The highest growth is 98.37 percent in FY 063/64 and the lowest is 31.01 percent in FY 062/63. This ratio is dependent upon the net loans to total assets (E_1). The problem of lower growth was due to delinquent loan and provision of adequate allowances for loan delinquency.

4.2.21 The growth in liquid investment over the five study period is fluctuating trend with the highest declining by 57.88 percent in FY 063/64 and the highest increasing by 1154.31 percent in FY 062/63. Since this ratio is dependent upon the liquid investment to total assets (E_2). Still, in FY 064/65 it was negative growth with 16.72 percent. Then, in FY 065/66 it was increased by 244.16 percent. The higher growth in two FY 062/63 and 065/66 shows that RCSL has paying less attention investing in liquid assets.

4.2.22 The growth in saving deposits of RCSL over the five study period is fluctuating trend with the highest growth by 111.75 percent in FY 062/63 and lowest growth by 29.31 percent in FY 064/65. Since this ratio is dependent upon the total saving deposits to total assets (E_5). The higher growth in saving deposits shows that the institution has a potentiality to invest in loan portfolio, which significantly generates more income.

4.2.23 The growth in members shares of RCSL over the five study period is fluctuating trend with the highest growth by 77.54 percent in FY 061/62 and the decreased by 0.17 percent in FY 065/66. Since this ratio is dependent upon the member shares capital to total assets (E_7). The higher growth in member shares capital shows that the institution has strong with paid-up capital and vice versa.

4.2.24 The growth in institutional capital of RCSL over the five study period is in decreasing trend. The highest growth is 346.43 percent in FY 061/62 and the lowest growth is 19.26 percent in FY 065/66. In FY 063/64 it was slightly increased to 115.99 percent from 115.20 percent of FY 062/63. The ratio is decreasing due to the low earnings over the periods.

4.2.25 Over the five year studies period, RCSL has been able to maintained the growth in membership within the PEARLS standard. The ratios are in decreasing trend in the study period. The highest growth is 54.87 percent in FY 061/62 and the lowest is 14.60 percent in FY 065/66.

CHAPTER FIVE
SUMMARY, CONCLUSION AND RECOMMENDATION

This chapter consists with three parts of the study - Summary, Conclusion and Recommendation. The first part deals with a summarization of the whole study, the second part depicts on the conclusion and finally the last part presents recommendation with the focus of its findings.

5.1 Summary

The study was conducted with the objective to analyze the financial performance of RCSL in the framework of PEARLS over the five years study period from FY 060/61 to 064/65 following a descriptive as well as analytical research design. The study is based on secondary data. Annual reports and other financial statements are used for the analysis of the study of RCSL as the major sources of data. The analysis of financial statement is done to obtain a better insight into a firm's position and performance. Various methodologies and tools have been applied to identify the financial position of institution and they act as accordingly ensuring the norms are appropriate with appraised by the PEARLS approach.

The major objective of the study was to analyze of financial performance of RCSL, which deals with the specific objectives of the study to know the trend in the protection, level of effective financial structure, trend in assets quality, rates of returns and costs, liquidity position and sign of growth of institution over the five years period.

PEARLS, is a financial performance monitoring system which determines the financial health of institution through the application of its indicators. The indicators of PEARLS were applied to find a better insight in terms of financial performance analysis of RCSL. These indicators were put forth to illustrate how change in one ratio has ramification for numerous other indicators. The financial performance of RCSL has been analyzed on the basis of PEARLS tools.

The various resources were incorporated in order to upsurge the conceptual review and to apparent a way to its purpose of research work. The concept of micro-finance, meaning and definition of cooperative, principles of cooperative, historical background and development of cooperative, organizational structure of cooperative, types of cooperative, rationale of financial performance analysis, historical background of RCSL, theoretical prescription and interlocking concept of PEARLS - protection, solvency, risk to solvency, concept of effective financial structure, concepts of assets, liabilities and institutional capital, concept of assets quality, concept of delinquency and its causes, implication and control, concept of non-earning assets and its financing, concept of rates of returns and costs, concept of loan portfolio, liquid and financial investments, concept of financial intermediation and administrative costs, concept of provision for loan losses, non-recurring income, concept of liquidity and concept of sign of growth were to a greater extent, embodied as conceptual review. On the other part, the review of articles and review of dissertations were included in the research review section.

The research study was undertaken with respect to time frame of five fiscal years from 060/61 to 064/65, to analyze the performance of RCSL within the framework of descriptive as well as analytical research design and the analysis therein has been made in the same way. To make a research study more reliable and accurate, RCSL has selected as this institution is running in a profitable drift compared to other Savings and Credit Cooperatives. The required data and information were collected from the secondary sources. In addition, primary data were also used in this research work if possible, which was collected by using unstructured interview with senior staff of the institution. In this research work, PEARLS ratio has been thoroughly implied of the collected data and information to get the meaningful result.

By the calculation of various ratios of RCSL comparing with PEARLS standard, the analysis has been made. In addition, the inflation has also been depicted as suggested by PEARLS in Nepalese scenario. The institution has adequately protected the loan loss with the provision of allowance. The consecutively increasing trend of loan delinquency is lower than that of the loan loss provision. The solvency of institution has consistently maintained within the PEARLS standard. The ratio of net loans to

total assets, liquid investment to total assets, saving deposits to total assets and member share capital to total assets is near about the PEARLS standard. The ratio of institutional capital to total assets is far below the PEARLS standard due to inability of generating adequate earnings. The delinquency ratio with respect to total loan portfolio is within the PEARLS standard. The ratio of non-earning assets to total assets is slightly higher the PEARLS standard due to high cash amount and increase in the acquisition of fixed assets. The net zero cost funds to non-earning assets ratio is far below the standard of PEARLS. Net loan income to average loan portfolio ratio is within the standard of PEARLS. It covers the cost of funds, cost of administration and operation, the cost of provisions and the cost of contribution with respect to its amount of investment in the loan portfolio. The ratio of liquid investment income to average liquid investment is quite low than the market rate. Cost on saving deposits to average saving deposits is above the inflation rates. The ratio of dividend paid on shares to average member shares over the following three years is within the PEARLS standard. The ratio of gross margin to total assets is consequently decreasing due to increase of interest cost on saving deposits and dividend paid on shares. The operating expenses to average total assets ratio is above the PEARLS standard but it is in decreasing trend. The provision for loan loss to average total assets ratio is satisfactory with controlled the delinquency in terms of loan portfolio. The ratio of non-recurring income to average total assets is minimal, which is within the PEARLS standard. The net income to average total assets is maintained in terms of E_9 but it is not adequate in terms of growth of total assets. The liquidity reserves to total deposit ratio is satisfactorily meet within the PEARLS standard. The ratio of non-earning liquid assets to total assets is above the standard of PEARLS. In loan portfolio it has satisfactory growth but not tune with increase in total assets and in liquid investment it has partial satisfactory. The growth in saving deposits, institutional capital and total assets of RCSL has satisfactorily increased as compared to PEARLS ratio.

In concise, though RCSL has been able to allocate the allowance for loan loss, satisfactorily maintained the solvency position, loan portfolio, liquid investment, saving deposits and member share capital up to its standard consecutively over the study periods, the institutional capital, non-earning assets and operating expenses has not been able to attain its standards. This is due to the poor assets, delinquent loan and

low earnings so as to enhance the total assets. The institution in the event of focusing primarily in savings deposits to invest in quality loan portfolio will substantially add up the institutional capital as a result of yielding earnings that shall, eventually ensures the sound financial health of RCSL.

5.2 Conclusion

Based on the study of its findings, the following conclusions have been taken as its final shape of the study on the financial analysis of Royal Cooperative Society Ltd. (RCSL) within the framework of PEARLS.

Protection (P)

Allowances for loan losses to allowances required for loan delinquent ratio reveals that the RCSL has been maintaining its standard as per PEARLS standard. It indicates that institution has allocated the adequate allowances in terms of loan delinquent and conducted the loan renewal policy against delinquent loan. It also indicates the institution has adequate earnings to defend any future losses. The reducing delinquency has been an area of sustained focus. The sign of growth in this ratio reveals the institution may face an acute problem in coming years. The solvency ratio of the institution shows that it was in quite standard of PEARLS. This is due to proportionately decreasing in delinquency and increasing in total savings, which consistently affected the total assets.

Effective Financial Structure (E)

The ratio of net loans to total assets is slightly higher than the PEARLS standard, which indicates that RCSL has maintained its standard as per PEARLS standard. The growth in loan portfolio in consequent years shows that the institution has potentiality to earn the income in coming years. RCSL has also maintained the liquid investment to total assets position within its standard. It shows that RCSL has managed the sources of funds effectively during the study period. The ratio of saving deposits also is slightly higher than the PEARLS standard. It is said that institution has able to collect the adequate saving deposits, which indicates its standard as per the PEARLS standard. The ratio of member share capital to total assets is partially with in the PEARLS standard. This ratio is in decreasing trend, which indicates that either it should be increase in member share capital or raise the external funds. The ratio of

institutional capital to total assets is falling the high below than the PEARLS standard. It shows that the institution has low earning.

Assets Quality (A)

The ratio of total loan delinquency to total loan portfolio is within the PEARLS standard, which indicates that RCSL has maintained its standard as per PEARLS standard. Due to this fluctuating ratio, the total loan delinquency has not been increased with respect to increase in total loan portfolio. This ratio may further decrease in coming year due to conduct the loan renewal policy against delinquent loan. The ratio of non-earning assets to total assets is above the PEARLS standard. This was due to investment in fixed assets and other assets. Due to lower net institutional capital, the ratio of net zero cost funds is far below the PEARLS standard.

Rate of Returns and Costs (R)

RCSL has managed to maintained net loan income to average loan portfolio ratio with the standard of PEARLS. It covers the cost of funds, cost of administration and operation, the cost of provisions and the cost of contribution with respect to its amount of investment in the loan portfolio. The ratio of liquid investment income to average liquid investment is quite low. The decreasing trend of gross spread ratio during the study period is due to increase of interest cost on saving deposits and dividend paid on shares. The decreasing trend of gross spread indicates the institution has low earning, it means low potentiality in future. The operating expenses to average total assets ratio in an average is high with the PEARLS standard. It means the institution paying the over expenditure but decreasing trend of this ratio shows to reduce of over expenditure. The ratio of loan loss provision to average total assets is within the PEARLS standard. It shows that the institution has adopted the good investment policy in loan portfolio and controlled the delinquency in terms of loan portfolio. The ratio of non-recurring income to average total assets is minimal and within the PEARLS standard. The net income to average total assets ratio shows that RCSL has been able to maintain the ratio of net income to average total assets in terms of E_9. But it is not adequate in terms of growth of total assets. It indicates that the institution is not encouraging to generate stable and safe earnings.

Liquidity (L)

The ratio of liquidity reserves to total deposits is slightly above the PEARLS standard. It shows that the institution has maintained the adequate amount of liquidity reserves with respect to total saving deposits, which affects the earning power of institution. Over the five years study period, the ratio of non-earning liquid assets to total assets is above the PEARLS standard. It is fluctuating during the study period.

Sign of Growth (S)

The growth in loans is harmony with the increase in total assets but not satisfactory as the ratio of net loans to total assets (E_1) is below the PEARLS standard. The growth in liquid investment is near about the standard as it is dependent upon with the ratio of liquid investment to total assets, E_2. The growth in saving deposits shows that RCSL has not satisfactorily able to maintain the standard with respect to E_5. It has unable to attract more depositors due to low cost of funds on saving deposits. The growth in member shares has in fluctuating trend over the study period, which reflects the satisfactorily maintained the standard with compared to E_7. The growth in institutional capital has in decreasing trend but within the PEARLS standard. It depends with the institutional capital to total assets, which are below the PEARLS standard. The growth in membership has in decreasing trend but within the PEARLS standard. The growth in total assets is within the PEARLS standard. RCSL has been able to maintain it above the inflation rates.

5.3 Recommendation

Due to the based on the above conclusions of the study, the following recommendations have been made as a suggestion to come up over the weakness as faced by RCSL for its sound financial health.

Protection (P)

The allowances for loan losses to allowances required for loan delinquent greater than 12 months have been maintained as per PEARLS standard. RCSL has allocated the adequate allowances in terms of loan delinquent and conducted the loan renewal policy against delinquent loan. The loan renewal policy against delinquent loan is the positive signal against delinquent loan. The solvency ratio is as per PEARLS

standard. The institution is advised to allocate the allowances for loan losses properly and strictly conduct the loan renewal policy against delinquent loan.

Effective Financial Structure (E)

The growth in loan portfolio in consequent years shows that the institution has potentiality to earn the income in coming years. RCSL is recommended to set optimal level of net loans to total assets in terms of liquid investments and the yield of this investment with regard to other investment alternatives. The liquid investment to total assets position is within its standard. It shows that RCSL has managed the sources of funds effectively during the study period. The ratio of saving deposits shows that institution has able to collect the adequate saving deposits. RCSL is recommended to maintain the ratio of liquid investment to total assets and saving deposits to total assets as per PEARLS standard. In terms of member share capital to total assets ratio, it is advisable to increase the member share capital as of total assets with in the PEARLS standard. Highly below institutional capital to total assets ratio shows that the institution has low earning. RCSL is recommended to increase the sufficient earning and manage it as per PEARLS standard.

Assets Quality (A)

The ratio of total loan delinquency to total loan portfolio is in control position within the PEARLS standard. The total loan delinquency has not been increased with respect to increase in total loan portfolio. This ratio may further decrease in coming year due to conduct the loan renewal policy against delinquent loan. In terms of non-earning assets to total assets ratio, it is recommended to institution to evaluate leasing alternatives against purchase or construction of fixed assets and establish depreciation and amortization policies in order to reduce the level of non-earning assets. In terms of zero cost funds to non-earning assets, it is advised to raise the institutional capital and control the non-earning assets to make it as the PEARLS standard.

Rate of Returns and Costs (R)

RCSL has maintained net loan income to average loan portfolio ratio in terms of its cost recovery. It covers the cost of funds, cost of administration and operation, the cost of provisions and the cost of contribution with respect to its amount of investment in the loan portfolio. It is recommended to the institution to increase the loan income with the set of different interest rates on loans according to their purpose, amount, term and risk. The ratio of liquid investment income to average liquid

investment is quite low. The institution needs to minimize the idle liquidity and liquidate non-earning assets and reinvest them in earning assets. The decreasing trend of gross spread ratio during the study period is due to increase of interest cost on saving deposits and dividend paid on shares. The institution has recommended that setting the interest rates with competitive on the financial market and manages the dividend payout ratio. It needs to increase the gross margin ratio by relying on quality assets that yield high earnings and control the loan portfolio from falling in delinquency. In terms of operating expenses to average total assets, the institution needs to eliminate unnecessary expenses and establish discipline in expenses of leadership and employee bodies. The ratio of loan loss provision to average total assets is within the PEARLS standard. It shows that the institution has adopted the good investment policy in loan portfolio and controlled the delinquency in terms of loan portfolio. The ratio of non-recurring income to average total assets is minimal and within the PEARLS standard. The net income to average total assets ratio shows that RCSL has been able to maintain the ratio of net income to average total assets in terms of E_9. But it is not adequate in terms of growth of total assets. It is recommended that the institution should encourage generating stable and safe earnings.

Liquidity (L)

The institution has maintained the adequate amount of liquidity reserves with respect to total saving deposits. The institution is to suggest that maintain the proper liquidity reserve as the PEARLS standard. The high-level liquidity reserve reflects that the institution has fall in idle cash or invested in low earning assets. So, it is either reinvested or controlled. In terms of non-earning liquid assets to total assets ratio, it is above the PEARLS standard. The institution should reduce or maintain the non-earning liquid reserve as per PEARLS standard.

Sign of Growth (S)

RCSL is to recommend that to readapt the policies and standards by competitive and worthwhile interest rates, amount to be granted, terms and purpose, leverage and security to increase the loan portfolio. The institution needs to focus in this segment according to its needs. The institution is recommended to increase the saving deposits

offering an attractive with competitive interest rate and should build up its credibility to attract the more depositors. It is advisable to control the delinquency and focus on reinvesting in productive assets in order to increase the level of institutional capital. The institution is recommended to focus on the saving deposits as the main source of growth in total assets and develop and effective marketing program to attract more savings. The total assets should be forcefully emphasized in the area where it contributes maximum gross spread.

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APPENDIX: PEARLS RATIOS

2.1: P: Protection

2.1.1: P_1: Allowance for Loan Losses to Allowances Required for Loans Delinquent > 1 Year

$$P_1 \text{ X} \frac{a}{b}$$

Where,

a = total allowances for loan losses
b = loan balances of all loans delinquent > 1 year

2.1.2: P_2: Net Allowance for Loan Losses to Delinquency of 1-12 months

$$P_2 \text{ X} \frac{a Z b}{c}$$

Where,

a = total allowances for loan losses
b = loan allowances for loan delinquent > 1 year
c = delinquency of 1-12 months

2.1.3: P_3: Total Write-off Delinquent Loans to Delinquent Loans > 1 Year

$$P_3 \text{ X} \frac{a}{b}$$

Where,

a = total write-off delinquent loans
b = loans delinquent > 1 year

2.1.4: P_4: Annual Loan Write-off to Average Loan Portfolio (Loan Write-off Ratio)

$$P_4 \text{ X} \frac{a Z b}{\frac{c \Gamma d}{2}}$$

Where,

a = accumulated loan write-off for current year
b = accumulated loan written of for previous year
c = gross loan portfolio as of current year-end
d = gross loan portfolio as of previous year-end

2.1.5: P_5: Accumulated Loan Recovery to Accumulated Loan Write-off (Recovery Ratio)

$$P_5 \text{ X} \frac{a}{b}$$

Where,

a = accumulated loan recovery
b = accumulated loan written

2.1.6: P_6: Net Value of Assets to Total Share and Deposits (Solvency Ratio)

$$P_6 \text{ X} \frac{a}{b}$$

Where,

a = net value of assets
b = sum of total savings and total share capital

Net Value of Assets

$$a \text{ X}[(c \Gamma d) \text{ Z} (e \Gamma f \Gamma g \text{ Z} h)]$$

Where,

c = total assets
d = allowances for risky assets
e = total loan loss provision for delinquent loan
f = total liabilities
g = problem assets
h = total deposits

2.2: E: Effective Financial Structure

2.2.1: E_1: Net Loan to Total Assets Ratio

$$E_1 \text{ X} \frac{a \text{ Z} b}{c}$$

Where,

a = gross loan portfolio
b = allowances for risky assets
(total loan loss provision)
c = total assets

2.2.2: E_2: Liquid Investment to Total Assets Ratio

$$E_2 \text{ X} \frac{a}{c}$$

Where,

a = total liquid investment
c = total assets

2.2.3: E_3: Financial Investment to Total Assets Ratio

$$E_3 \text{ X} \frac{a}{c}$$

Where,

a = total financial investment
c = total assets

2.2.4: E_4: Non-financial Investment to Total Assets Ratio

$$E_4 \text{ X} \frac{a}{c}$$

Where,

a = total non-financial investment
c = total assets

2.2.5: E_5: Saving Deposits to Total Assets Ratio

$$E_5 \, X \frac{a}{c}$$

Where,

a = total saving deposits
c = total assets

2.2.6: E_6: External Credit to Total Assets Ratio

$$E_6 \, X \frac{a}{c}$$

Where,

a = external credit
c = total assets

2.2.7: E_7: Member Share Capital to Total Assets Ratio

$$E_7 \, X \frac{a}{c}$$

Where,

a = member share capital
c = total assets

2.2.8: E_8: Institutional Capital to Total Assets Ratio

$$E_8 \, X \frac{a}{c}$$

Where,

a = institutional capital
c = total assets

2.2.9: E_9: Net Institutional Capital to Total Assets Ratio

$$E_9 \, X \frac{a}{c}$$

Where,

a = net institutional capital
c = total assets

Net Institutional Capital (a)

$$a \, X(d \, \Gamma \, e) \, Z(f \, \Gamma \, 0.35g)$$

Where,

d = institutional capital
e = allowances for risky assets
f = outstanding loans delinquent > 1 year
g = outstanding loans delinquent < 1 year

2.3: A: Asset Quality

2.3.1: A_1: Total Loan Delinquency to Total Loan Portfolio

$$A_1 \, X \frac{a}{b}$$

Where,

a = total delinquent loan (loan past due for one month and more than one month)

b = total loan portfolio

2.3.2: A_2: Total Non-earning Assets to Total Assets Ratio

$$A_2 \, X \frac{a}{b}$$

Where,

a = total non-earning assets

b = total assets

Total Non-earning Assets (a)

$$a \, X(c \, \Gamma \, d \, \Gamma \, e \, \Gamma \, f \, \Gamma \, g \, \Gamma \, h)$$

Where,

c = cash on hand

d = non-interest bearing monetary checking account

e = account receivables

f = assets in liquidation

g = fixed assets (land & building, equipment etc.)

h = prepaid expenses and other deferrals

2.3.3: A_3: Net Zero Funds to Total Non-earning Assets Ratio

$$A_3 \, X \frac{a}{b}$$

Where,

a = net zero cost funds

b = total non-earning assets

Net Zero Funds (a)

$$a \, X(c \, \Gamma \, d \, \Gamma \, e)$$

Where,

c = total net institutional capital

d = total transitory capital

e = total non-interest bearing liabilities

2.4: R: Rates of Return and Costs

2.4.1: R_1: Net Loan Income to Average Net Loan Ratio

$$R_1 \text{ X} \frac{a \text{Z} b}{\frac{c \Gamma d}{2}}$$

Where,

a = total loan income (including commission, fees and penalty interest)
b = insurance premium paid on loans
c = net loan portfolio as of current year-end
d = net loan portfolio as of previous year-end

2.4.2: R_2: Liquid Investment Income to Average Liquid Investment Ratio

$$R_2 \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = total liquid investment income during the year
b = total liquid investment as of current year-end
c = total liquid investment as of previous year-end

2.4.3: R_3: Financial Investment Income to Average Financial Investment Ratio

$$R_3 \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = total financial investment income during the year
b = total financial investment as of current year-end
c = total financial investment as of previous year-end

2.4.4: R_4: Non-financial Investment Income to Average Non-financial Investment Ratio

$$R_4 \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = total non-financial investment income during the year
b = total non-financial investment as of current year-end
c = total non-financial investment as of previous year-end

2.4.5 R_5: Total Interest Cost on Saving Deposits to Average Saving Deposits Ratio

$$R_5 \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = total saving deposit cost and it includes total interest paid on saving deposits, total interest premium paid on saving deposits, total tax paid by MFIs on saving deposit interest
b = total saving deposits as of current year-end

c = total saving deposits as of previous year-end

2.4.6: R_6: Total Interest Cost on External Credit to Average External Credit Ratio

$$R_6 \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = total interest paid on external credit (borrowed funds)
b = total external credit (borrowed funds) as of current year-end
c = total external credit (borrowed funds) as of previous year-end

2.4.7: R_7: Total Dividend on Share Capital to Average Member Share Capital Ratio

$$R_7 \text{ X} \frac{(a \Gamma b \Gamma c)}{\frac{d \Gamma e}{2}}$$

Where,

a = total dividend paid on member shares
b = total insurance premium paid on member share capital
c = total taxes paid by MFI on dividend on share
d = total member share capital as of current year-end
e = total member share capital as of previous year-end

2.4.8: R_8: Gross Margin to Average Total Assets Ratio

$$R_8 \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = gross margin
b = total assets as of current year-end
c = total assets as of previous year-end

Gross Margin (a)

$$a \text{ X}(d \Gamma e \Gamma f \Gamma g \Gamma h) \text{ Z}(i \Gamma j \Gamma k)$$

Where,

d = loan interest income
e = liquid investment income
f = financial investment income
g = non-financial investment income
h = other income
i = interest cost of saving deposits
j = dividend cost of member share capital
k = interest cost of external credit (borrowed funds)

2.4.9: R_9: Operating Expenses to Average Total Assets Ratio

$$R_9 \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = total operating expenses excluding provision for loan losses
b = total assets as of current year-end
c = total assets as of previous year-end

2.4.10: R_{10}: Total Loan Loss Provision Expenses to Average Total Assets Ratio

$$R_{10} \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = total loan loss provision expenses of current year for all risky assets
b = total assets as of current year-end
c = total assets as of previous year-end

2.4.11: R_{11}: Total Non-recurring Income to Average Total Assets Ratio

$$R_{11} \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = total non-recurring income of current year
b = total assets as of current year-end
c = total assets as of previous year-end

2.4.12: R_{12}: Net Income to Average Total Assets Ratio

$$R_{12} \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

Where,

a = net income after dividend
b = total assets as of current year-end
c = total assets as of previous year-end

2.5: L: Liquidity

2.5.1: L_1: Short-term Investment + Liquid Assets - Short-term Payables to Total Saving Deposits Ratio

$$L_1 \text{ X} \frac{(a \Gamma b \text{ Z} c)}{d}$$

Where,

a = total earning liquid investment
b = total non-earning liquid investment
c = total short-term payables < 30 days
d = total saving deposits

2.5.2: L_2: Liquid Reserve to Total Saving Deposits Ratio

$$L_2 \text{ X} \frac{(a \Gamma b)}{c}$$

Where,

a = total earning liquid reserve
b = total non-earning liquid reserve
c = total saving deposits

2.5.3: L_3: Non-earning Liquid Assets to Total Assets Ratio

$$L_3 \text{ X} \frac{a}{b}$$

Where,

a = total non-earning liquid assets
b = total assets

2.6: S: Sign of Growth

2.6.1: S_1: Growth in Gross Loan

$$S_1 \text{ X } \frac{a}{b} \text{ X} 100 \text{ Z} 100$$

Where,

a = total gross loan as of current year-end
b = total gross loan as of previous year-end

2.6.2: S_2: Growth in Liquid Investment

$$S_2 \text{ X } \frac{a}{b} \text{ X} 100 \text{ Z} 100$$

Where,

a = total liquid investment as of current year-end
b = total liquid investment as of previous year-end

2.6.3: S_3: Growth in Financial Investment

$$S_3 \text{ X } \frac{a}{b} \text{ X} 100 \text{ Z} 100$$

Where,

a = total financial investment as of current year-end
b = total financial investment as of previous year-end

2.6.4: S_4: Growth in Non-financial Investment

$$S_4 \text{ X } \frac{a}{b} \text{ X} 100 \text{ Z} 100$$

Where,

a = total non-financial investment as of current year-end
b = total non-financial investment as of previous year-end

2.6.5: S_5: Growth in Saving Deposits

S_5 X $\frac{a}{b}$ X100 Z100

Where,

a = total saving deposits as of current year-end
b = total saving deposits as of previous year-end

2.6.6: S_6: Growth in External Credit

S_6 X $\frac{a}{b}$ X100 Z100

Where,

a = total external credit as of current year-end
b = total external credit as of previous year-end

2.6.7: S_7: Growth in Member Share

S_7 X $\frac{a}{b}$ X100 Z100

Where,

a = total member share as of current year-end
b = total member share as of previous year-end

2.6.8: S_8: Growth in Institutional Capital

S_8 X $\frac{a}{b}$ X100 Z100

Where,

a = total institutional capital as of current year-end
b = total institutional capital as of previous year-end

2.6.9: S_9: Growth in Net-institutional Capital

S_9 X $\frac{a}{b}$ X100 Z100

Where,

a = total net institutional capital as of current year-end
b = total net institutional capital as of previous year-end

2.6.10: $S_{10.}$: Growth in Membership

$S_{10.1}$: Growth in Founder Members

$S_{10.1}$ X $\frac{a}{b}$ X100 Z100

Where,

a = total founder members as of current year-end
b = total founder members as of previous year-end

$S_{10.2}$: Growth in General Members

$S_{10.2}$ X $\frac{a}{b}$ X100 Z100

Where,

a = total general members as of current year-end
b = total general members as of previous year-end

2.6.11: S_{11}: Growth in Total Assets

$$S_{11} \text{ X } \frac{a}{b} \text{ X} 100 \text{ Z} 100$$

Where,

a = total assets as of current year-end
b = total assets as of previous year-end

APPENDIX 4.1

Solvency Ratio (P_6)

(NRs. '000)

P_6	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Net Value of Assets	9130	19378	25523	33070	60290
b. Total Shares and Deposits	9160	19396	25476	32944	60085

Source: **Annual Reports, BCSL**

Calculation,

$$P_6 \text{ X} \frac{a}{b}$$

$$\text{X} \frac{9130}{9160} \qquad \text{X} 0.9967 \qquad \text{X} 99.67\,\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.2

Net Loans to Total Assets (E_1)

(NRs. '000)

E_1	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64

a.	Total Gross loan Portfolio outstanding	10277	12451	24553	34404	56048
b.	Total Allowance for Loan losses	22	60	142	256	368
c.	Total Assets	11743	22657	30058	39955	69377

Source: **Annual Reports, BCSL**

Calculation,

$$E_1 = \frac{(a - b)}{c}$$

$$= \frac{(10277 - 22)}{11743} = \frac{10255}{11743} = 0.8733 = 87.33\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.3

Saving Deposits to Total Assets (E_5)

(NRs. '000)

E_5		Fiscal Year				
		059/60	060/61	061/62	062/63	063/64
a.	Total Saving Deposits	9160	19396	25476	32944	60085
b.	Total Assets	11743	22657	30058	39955	69377

Source: **Annual Reports, BCSL**

Calculation,

$$E_5 = \frac{a}{b}$$

$$= \frac{9160}{11743} = 0.78004 = 78.00\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.4

Table 4.8: Institutional Capital to Total Assets (E_8)

(NRs. '000)

E_8	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Institutional Capital	125	269	581	893	1065
b. Total Assets	11743	22657	30058	39955	69377

Source: **Annual Reports, BCSL**

Calculation,

$$E_8 \text{ X} \frac{a}{b}$$

$$\text{X} \frac{125}{11743} \quad \text{X}0.01064 \quad \text{X}1.06\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.5

Net Institutional Capital to Total Assets (E_9)

(NRs. '000)

E_9	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Net Institutional Capital	96	250	628	1019	1270
b. Total Assets	11743	22657	30058	39955	69377

Source: **Annual Reports, BCSL**

Calculation,

$$E_9 \text{ X} \frac{a}{b}$$

$$\text{X} \frac{96}{11743} \quad \text{X}0.00818 \quad \text{X}0.82\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.6

Net Zero Funds to Total Non-earning Assets (A_3)

(NRs. '000)

A_3	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Net Zero Cost Funds	96	250	628	1019	1270
b. Non-earning Assets	782	1614	1886	2486	2901

Source: **Annual Reports, BCSL**

Calculation,

$$A_3 \text{ X} \frac{a}{b}$$

$$\text{X}\frac{96}{782} \qquad \text{X}0.12276 \qquad \text{X}12.28\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.7

Net Loan Income to Average Loan Portfolio (R_1)

(NRs. '000)

R_1	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Net Loan Income	2427	2915	4673	6110	8388
b. Net Loan Portfolio as of Current year-end	10254	12391	24411	34148	55680
c. Net Loan Portfolio as of Last year-end	7185	10254	12391	24411	34148

Source: **Annual Reports, BCSL**

Calculation,

$$R_1 \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

$$X\frac{2427}{\frac{10254\Gamma 7185}{2}} \quad X0.27834 \quad X27.83\%`$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.8

Total Gross Margin to Average Total Assets (R_8)

(NRs. '000)

R_8	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Total Gross Margin	1618	1529	2303	2334	3085
b. Total Assets as of Current year-end	11743	22657	30058	39955	69377
c. Total Assets as of Last year-end	8948	11743	22657	30058	39955

Source: **Annual Reports, BCSL**

Calculation,

$$R_8\ X\frac{a}{\frac{b\Gamma c}{2}}$$

$$X\frac{1618}{\frac{11743\Gamma 8948}{2}} \quad X0.15639 \quad X15.64\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.9

Provision for Loan Losses to Average Total Assets (R_{10})

(NRs. '000)

R_{10}	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64

a.	Total Loan loss Provision	22	60	142	256	368
b.	Total Assets as of Current year-end	11743	22657	30058	39955	69377
c.	Total Assets as of Last year-end	8948	11743	22657	30058	39955

Source: **Annual Reports, BCSL**

Calculation,

$$R_{10} \text{ X} \frac{a}{\frac{b \Gamma c}{2}}$$

$$\text{X} \frac{22}{\frac{11743 \Gamma 8948}{2}} \qquad \text{X}0.002126 \qquad \text{X}0.21\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.10

Net Income to Average Total Assets (R_{12})

(NRs. '000)

	R_{12}	Fiscal Year				
		059/60	060/61	061/62	062/63	063/64
a.	Net Income	119	254	546	761	747
b.	Total Assets as of Current year-end	11743	22657	30058	39955	69377
c.	Total Assets as of Last year-end	8948	11743	22657	30058	39955

Source: **Annual Reports, BCSL**

Calculation,

$$R_{12}\ X\frac{a}{\frac{b\Gamma c}{2}}$$

$$X\frac{119}{\frac{11743\Gamma 8948}{2}} \qquad X0.0115 \qquad X1.15\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.11

Liquidity Reserve to Total Saving Deposits (L_2)

(NRs. '000)

L_2	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Total Earning Liquid Reserve	685	8592	3619	3014	10373
b. Total Non-earning Liquid Reserve	293	806	450	918	1083
c. Total Saving Deposits	9160	19396	25476	32944	60085

Source: **Annual Reports, BCSL**

Calculation,

$$L_2\ X\frac{(a\ \Gamma\ b)}{c}$$

$$X\frac{(685\ \Gamma\ 293)}{9160} \qquad X0.10677 \qquad X10.68\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.12
Growth in Loans (S_1)

(NRs. '000)

S_1	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64

a. Gross Loan Portfolio as of Current year-end	10277	12451	24553	34404	56048
b. Gross Loan Portfolio as of Last year-end	7185	10277	12451	24553	34404

Source: **Annual Reports, BCSL**

Calculation,

$$S_1 \text{ X } \frac{a}{b} X100 \text{ Z}100$$

$$\text{X } \frac{10277}{7185} X100 \text{ Z}100 \qquad \text{X}0.4303 \qquad \text{X}43.03\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.13

Growth in Saving Deposits (S_5)

(NRs. '000)

S_5	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Total Saving Deposits as of Current year-end	9160	19396	25476	32944	60085
b. Total Saving Deposits as of Last year-end	6066	9160	19396	25476	32944

Source: **Annual Reports, BCSL**

Calculation,

$$S_5 \text{ X } \frac{a}{b} X100 \text{ Z}100$$

$$\text{X } \frac{9160}{6066} X100 \text{ Z}100 \qquad \text{X}0.51006 \qquad \text{X}51.01\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.14

Growth in Members Share Capital (S_7)

(NRs. '000)

S_7	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Total Member Share as of Current year-end	2047	2293	2737	3527	3521
b. Total Member Share as of Last year-end	1153	2047	2293	2737	3527

Source: **Annual Reports, BCSL**

Calculation,

$$S_7 \text{ X } \frac{a}{b} X100 \text{ Z}100$$

$$\text{X } \frac{2047}{1153} X100 \text{ Z}100 \qquad \text{X}0.77537 \qquad \text{X}77.54\%$$

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.15

Growth in Institutional Capital (S_8)

(NRs. '000)

S_8	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Total Institutional Capital as of Current year-end	125	269	581	893	1065
b. Total Institutional Capital as of Last year-end	28	125	269	581	893

Source: **Annual Reports, BCSL**

Calculation,

S_8 X $\frac{a}{b}$ X100 Z100

X $\frac{125}{28}$ X100 Z100 X3.46428 X346.43 %

The ratios for remaining period have been calculated accordingly.

APPENDIX 4.16

Growth in Total Assets (S_{11})

(NRs. '000)

S_{11}	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
a. Total Assets as of Current year-end	11743	22657	30058	39955	69377
b. Total Assets as of Last year-end	8948	11743	22657	30058	39955

Source: **Annual Reports, BCSL**

Calculation,

S_{11} X $\frac{a}{b}$ X100 Z100

X $\frac{11743}{8948}$ X100 Z100 X0.31236 X31.24 %

The ratios for remaining period have been calculated accordingly.

APPENDIX 1.1

ROYAL COOPERATIVE SOCIETY LTD.

POKHARA, KASKI

Balance Sheet

Liabilities and Assets	Fiscal Year				
	059/60	060/61	061/62	062/63	063/64
Capital and Liabilities					
Share/Paid-up Capital	2047000.00	2292500.00	2736500.00	3526600.00	3521000.00
Saving Deposits	9159922.49	19395842.21	25476240.09	32944054.74	60085319.18
Account Payable	389024.07	640136.37	1122460.82	2334887.55	4337151.20
Reserve /Provision Fund/P&L					
General Reserve Fund	36836.78	100456.94	236910.71	427247.72	614048.75
Institutional Reserve Fund	27627.58	48932.70	106273.03	143025.79	141126.56
Staff Welfare Fund	16576.55	30705.62	61404.20	85651.66	84262.67
Dividend Fund	22102.07	46904.17	82521.43	114202.21	113631.85
Cooperative Education Fund	11051.03	19592.08	50528.21	62979.32	56040.31
Development Fund	11051.03	22137.08	43073.22	59674.32	56040.31
Loan loss Provision	22102.07	60274.17	142146.43	256348.64	368429.26
Total Capital & Liabilities	***11743293.67***	***22657481.34***	***30058058.14***	***39954671.95***	***69377050.09***
Assets					
Cash	292789.00	806302.00	449521.00	917770.00	1083011.00
Bank	684951.04	8591921.15	3619091.74	3014114.73	10373357.88
Account Receivable	93104.50	434791.43	660712.31	871582.71	1096310.39
Advance	50000.00	50000.00	-	-	-
Share Investment	-	-	-	50000.00	55000.00
Loan Investment					
Business loan	7679846.45	9434756.17	14337329.25	15032150.90	16790704.10
Hire purchase loan	2389751.43	2471406.88	7974146.05	13679361.37	21403278.37
Housing loan	-	-	1042793.60	2512372.71	3610432.58
Deposit loan					
Fixed deposit loan	207000.00	544957.70	50000.00	1000986.30	941919.93
Regular Saving deposit loan	-	-	1137786.63	2179564.89	7094149.20
Miscellaneous loan	-	-	11000.00	-	6207590.90
Fixed Assets	345851.25	323346.01	775677.56	696768.34	721295.74
Total Assets	***11743293.67***	***22657481.34***	***30058058.14***	***39954671.95***	***69377050.09***