CHAPTER-I

INTRODUCTION

1.1 Background

Nepal is developing country. It lacks capital for economic development and growth of country. Economic development is means to achieve prosperity and peace. So, capital formation and its utilization are vital for sustainable economic growth of country. For the purpose government formulates various plans, policies and programmes. In this context government had promulgated various liberal policies time to time. The liberal policy was extended even in financial sectors. In 1980's government introduced "Financial Sector Reforms" to encourage and assist to establish commercial banks and financial institutions. Since the introduction of reform many privately owned and joint ventured banks were established and it is still a trend. Before 2041 B.S. there were only two commercial banks in existence. These two banks were unable to meet the demands of people and they were insufficient for proper utilization of resources so new banks with modern amenities and equipment and proper management were highly sought and in consequences thereof, country observed emergence of large number of private commercial banks, development banks, finance companies etc.

Role of commercial bank and financial institution in the economic development of country is indisputable. They are backbone of country's economy. Commercial banks and financial institution help the process of resource mobilization. Commercial banks and financial institutions help the process of resources by mobilizing the from surplus units and in turn lend these funds to deficient units. In this way the commercial banks provide savers highly liquid, divisible assets at a lower risk while the investors receive a large pool of resources. Satisfaction of both lender's and borrower preference determines the success of intermediary function of an economy. The banking sector is largely responsible for collecting household savings in terms of different types of deposits and regulating them in the society by lending these to various sectors and by holding government securities. The banking sector has now reached to the most remotes areas of the country and has experienced a good deal in the growth of the economy. The lending of their resources in small-scale industries under intensive banking programme has enabled the banks to share in the economic growth of the country. Their lending in priority sectors is according to small industry regulations because of which the banks have to lend certain percentage of their deposit in those sectors regardless of the income (repayment) from it.

These financial institutions are often fragile and susceptible to failure because of poor management, particularly financial management. Deposit collected by these financial institutions are lend as loan and advances in various sectors in the form of investment, short term loan, long term loan etc. these loans and advances vital for profitability of banks and also proper utilization of resources of country as well as capital formation for investors. It is supposed that repayment of interest or principal shall have to be served without any impediment but unfortunately some time these loan and advances borrowed by investors become unproductive because of risk underlying in the particular business. They become unable to repay loan. So such loan may be considered as doubtful and bad loan. This bad loan and doubtful loan is known as Non-performing assets or loan in short NPA\NPL. It could have adverse effect in bank's profitability both through loss of interest income and write off the principle loan amount. Profitability is desired stage for any type of business enterprises so banks are not exceptional. However increasing non-performing assets have the direct impacts on bank's profitability, as legally banks are not allowed to book income an such accounts and at the same since banks are forced to make provision on such assets.

Beside risk underlying in the business other factors also effects in the increment of non-performing loan. These are attitude of the borrower, types and quality of collateral taken and legal complication created by the borrower during the loan recovery process. Reduction of NPA has always been a major problem for ever commercial bank in recent days. NPA management has been the top priority for banks. As easier, said than done, it's always been nerve-racking task for banks and whole banking industry now is struggling to get rid of it through various means.

Performing assets are those that repay principal and interest to the bank. These assets constitute the primary source of income to banks. Banks are willing to lend as much as possible. However, they have to careful about the safety of such loans. Loans are risky assets, even though bank lends most of its resources in loans.

"Loan and advances dominate the assets the assets side of the balance sheet of any bank. Similarly, earning from such loan and advances occupy a major space in income statement of the banks. However, it is very important to be remained that most of the bank failure in the world due to shrinkage on the value of the loan and advance. Here loan is known as risky assets. Risk of non-repayment of loan is known as credit risk or default risk. Performing loans have multiple benefits to the society while non-performing loan erodes even existing capital" (*Pradhan; 1994:17).*

The operating of the banking institutions has been governed by the government rules and regulation, international industry norms, relevant acts, Memorandum of Association(MOA),Article of Association(AOA), instruction given at the time of getting intent and Directives issued by Central bank from time to time. Similarly, the expectation of the stakeholder should also be taken into consideration. All banking institution is supposed to confine their activities within the stated framework.

1.1.1 Commercial Banks

Historically, a bank may have been evolved from a business which dealt in the precious metals or in the remittance of money from one country to another, or which offered its services as an intermediary to arrange loans or for the safe custody of valuables, or which borrowed the savings of the public on the security of its reputation and then invested there at its own discretion and at its own risk. Bank is as old as trade itself. The simplest form of banking was probably money changing, which was an elementary form of foreign-exchange banking systems of money lending, credit and interest were established in southwestern Asia more than 4000 years ago. However, banking in its modern form is since the A.D. 1100s. It developed when traders gained excess profits, when many people wanted to keep their valuable safe and when rulers had to borrow money to pay for wars and other ventures. The first banks were in the grate centers of international trade in the middle ages. These centers were in Italy, on the western shores of the Mediterranean and in the coastal areas of northern Western Europe. General banking practice developed most rapidly in Italy. One of the earliest Italian banks was the Vitale of Venice, formed in 1157. it was formed as a result of a forced loan made by merchants to the government of Venice, and it handled only government debt. The earliest deposit bank in Europe was the Taula di Cambia in Barcelona, Spain, established in 1401. Medieval banking developed most in Florence, Italy, and was closely connected with the wool trade.

In 1587, the first public bank was established. It was Bank of Venice, also known as the Banco Di Rialto or Banco della Piazza. The business of the bank of Venice was entirely separate from merchant trading. Economists regard the Bank of Venice a having started the era of modern banking.

The spread of Banking through Europe was rapid from the late 1600s onwards. In 1609, the Bank of Amsterdam was founded in Netherlands, in imitation of the Bank of Venice.

1.1.2 Evolution of Banking Industry in Nepal

The development of banking industry in Nepal has not long history as compared to other developed countries of the world. At ancient period, landlords, moneylenders, merchant, goldsmith etc were played the role of the bank. Though establishment of banking industry was very recent, some crude banking operations were in practice even in the ancient times. In the context of Nepal, Prime Minister Ranodip Singh established “Tejarath Adda" during the year 1880 A .D. which was the first step in institutional development of banking. Tejarath Adda did not collect deposit from public but granted loan to public against the collateral of bullions. Thus in the absence of saving mobilizing, "Adda" faced financial problems making it impossible to cater to the credit need of general population throughout the country. Consequently the major parts of, the country remain untouched from these limited banking activities. In addition, in 1991 BS, for the welfare of government staff, "Sainik Drabya Kosh" was established. The development of trade with India and other countries increase the necessity of the institutional banker, which can act more widely to enhance the trade and commerce and to touch the remote non-banking sector in the economy. Reviewing this situation, the "Udhyog Parishad"(Industrial Development Board) was constituted in 1936 A.D. year after its establishment, it formulated the, company Act,, and, Nepal Bank Act" in 1937 A.D under which Nepal Bank limited was established in 1937 BS with Government sharing 5l percent and private sector sharing 49 percent. This was a mild stone in the foundation of modern banking system of Nepal.

Modern banking practices emerged with the establishment of Nepal Bank Limited .However the standard of Nepal Bank Limited alone in total monetary and financial sector was not sufficient and satisfactorily. Thus Nepal Rastra Bank was setup on 20l3/0l/l4 as a central bank under Nepal Rastra Bank Act 2012 BS Similarly on 2022.10.10 Rastriya Banijya Bank was established as fully government owned commercial banks. With the emergence of RBB, banking service spread to both the urban and rural areas but customers failed to have taste of quality/competitive service because of excessive political and bureaucratic interference. With the concept of industrial development of the nation, industrial Development Centre was set in 2013 B.S. which was converted to Nepal Industrial Development Corporation in 2016 BS. Similarly, to develop and support agricultural products so that agricultural productivity could be enhanced through introduction of modern agricultural techniques, Agricultural Development Bank (ADB) was established in 2024/10/07. As liberalization, privatization and Globalization have emerged as a new super power all over the world and Nepalese economy also adopted the same during the 1980s. as a result, Nabil Bank Limited (erstwhile Nepal Arab Bank Limited) was established I 2041/03/29, which opened the door of opening commercial banks to the private sector. Nabil Bank Limited emerged as the first joint venture bank when the banking industry is totally dominated by Government and semi-government banks mainly to revitalize the economy by accelerating productivity in various sectors and to provide efficient customer service. Having observed the success on Nabil based on marketing concept and also because of liberal economic policy adopted by the successive government, many commercial banks have been established all over the kingdom. Following is the list of commercial banks that have been came into existence in Nepalese banking industry after liberalization policy adopted by the nation as 15 July 2004.

1.1.3 Sample Banks

Nabil Bank Limited

Nabil Bank was formerly known as Nepal Arab Bank Limited was established in July' 12th 1984 under a technical service agreement with Dubai Bank Ltd., Dubai which was later merged with Emirates Bank, UAE. It is the pioneer joint venture Bank of Nepal. Nabil is the only joint venture bank with 17 points of representing Nepal registering strong growth in the balance sheet performance as well as profits year after year. The initial capital of Rs. 30 million has gone to Rs. 1314 million as at mid-July 2003. Nabil launched its operation with the marketing concept. Nabil has also been pioneer in introducing modern banking and innovative products in Nepal like consortium finance, credit card etc. Nabil is the sole bank to a multitude of international aid agencies, NGOs, Embassies and Consultancy in Nepal. Nabil has been providing wide range of banking services to various parts of the society. Nabil bank ranks among the top three financial institutions in Nepal in terms of markets share of handling Nepal's trade. Nabil bank has been managed by a team of qualified and highly experienced professionals.

Standard Charted Bank Limited

Standard Chartered Bank Limited was formerly known as Grindlay’s Bank. It was established in 1987 AD. Standard Chartered Bank Nepal Limited has been in operation in Nepal since 1987 when it was initially registered as a joint venture operation. Today the Bank is an integral part of Standard Chartered Group who has 75%o ownership in the company with 25% shares owned by the Nepalese public. The Bank enjoys the status of the largest international bank currently operating in Nepal. Standard Chartered Group employs almost 60,000 people, representing nearly 100 nationalities in over 50 countries in the Asia Pacific Region, South Asia, the Middle East, Africa, the United Kingdom and the Americas. This diversity lies at the heart of the Bank's values and supports the Bank's growth as the world increasingly becomes one market.

With strong organic growth supported by strategic alliances and acquisitions and driven by its strengths in the balance and diversity of its business, products, geography and people, Standard Chartered is well positioned in the emerging trade corridor of Asia and the Middle East.

An integral part of the only international banking Group currently operating in Nepal, the Bank enjoys an impeccable reputation of a leading financial institution in the country. With 15 points of representation and 16 ATMs across the Kingdom and with around 350 local staff, Standard Chartered Bank Nepal

Ltd. is in a position to serve its customers through a large domestic network. In addition to which the global network of Standard Chartered Group gives the Bank a unique opportunity to provide truly international banking in Nepal.

Standard Chartered Bank Nepal Limited offers a full range of banking products and services in Wholesale and Consumer banking, catering to a wide range of customers encompassing individuals, mid-market local corporate, multinationals, large public sector companies' government corporations, airlines, hotels as well as the DO segment comprising of embassies, aid agencies, NGOs and INGOs.

The Bank has been the pioneer in introducing 'customer focused' products and Services in the country and aspires to continue to be a leader in introducing new products in delivering superior services. It is the first Bank in Nepal that has implemented the Anti-Money Laundering policy and applied the 'Know Your Customer procedure on all the customer accounts.

1.2 Focus of the Study

The main focus of this study will be to know about the non-performing assets of selected Nepalese commercial banks and make comparison study of non-performing assets of selected commercial banks.

Credit policy of any commercial banks is major policy because it affects overall health of commercial banks. So commercial banks are aware about credit policy. They are cautious while issuing loan and advances. Nevertheless still banks have to face NPAs. Most commercial banks are facing this problem and it is increasing. This study mainly focuses on non-performing loans or assets of selected commercial banks.

1.3 Statement of the Problem

Commercial banks are indispensable institutions which act as intermediately between lender and borrower. These institutions are necessary to assist in economic growth and economic development. Any country in the world strives for economic growth and economic development because it is distinct mean for wholesome development of country. Aspiration of people for peace and prosperity is possible only if economic growth and economic development continues in wholesome manner in country.

Commercial banks collect money from depositors in small amount to huge amount these deposited money are disbursed to borrowers as loan advances. These loan and advances are capital for business enterprises. So repayment of loan and advances to banks as principle and interest depends upon the economic and financial health of these business enterprises.

Besides the economic and financial health of these enterprises, the attitude of owner, legal practices of the land etc also effects in the repayment of loan and advances. The underlying collateral also effect in the repayment or compensation of loan and advances.

Financial institutions operating in Nepal have to undergo various kinds of problems. They have limited investment opportunities. The available opportunities are also competitive because of existence of many commercial banks. The credit extended by the commercial banks to agriculture and industrial sector is not satisfactory to meet the present growing need of the development of the country. Nepotism and political influence also effects the investment decision of the commercial banks. Granting loans against insufficient deposit, overvaluation of goods pledged, land building mortgaged, risk averting decision regarding loan recovery and negligence in recovery of overdue loan is some of the basic loopholes and the unsound investment policy sighted in the banks.

Therefore, investment of commercial bands is not that productive. This has caused various problems to commercial banks. Timely repayment of loan is always expected by commercial banks from borrowers but it is dwindling. As a result bad debt and not-performing assets are increasing which has invited the rise to NPA. This NPA has many implications in the banks. First, it directly affects profitability of commercial banks. On the other hand, they get loss in their investment.

Specifically this study is connected to search answer of the following questions related to the selected Banks.

- What is the trend and actual level of NPA in Nepalese commercial banks?
- Is the NPA is affecting the financial performance in this sector?
- Is the regulation and policy framework of NRB is sufficient to control NPA level?
- What are the causes of the increment of NPA?
- Is the present level is satisfactory in Nepalese financial sector?
- What are the guidelines of provisions pertaining to loan classification and loan loss provision and are Nepalese Commercial Banks a practicing NRB's regulation/directives regarding loan loss provision for non-performing loan or not?
- What is the overall effect of NPA on the profitability of the selected Banks?

1.4 Objectives of Study

The major objective of this research is to examine the level of non-performing assets (NPAs). The specific objectives are:

- To evaluate the proportion of non-performing loan and the level of NPAs in total deposit and total lending in the selected commercial banks.

- To evaluate the relationship between loan amount provided by commercial banks provided and loan loss provision in the commercial banks.
- To analyze the impact of non-performing assets in the profit of commercial banks.
- To present the trend line of the non-performing assets, loan and advances, loan loss provision of selected commercial banks.

1.5 Significance of the Study

NPA is becoming prominent problem in commercial banks. Good investment policy of the bank has positive impact on economic development of the country and vice versa. But due to various reasons investment policy of commercial banks are not effective and productive. Non-productive loan increases non-performing assets and non-performing loans. This increases loan loss provision according to the directive of Nepal Rastra Bank, central bank. The portfolio of loan provision and loan loss provision affect its overall financial strength of the banks. This research is conducted to highlight present issues regarding non-performing and loan loss provision.

There are some researchers conducted on NPAs concerning various commercial banks in Nepal. They have conducted research just to show the NPA position in various commercial banks. But this research will compare NPA status and its effects in various aspects of their major act ivies like loan lending, deposit collection etc. between private bank and government bank.

1.6 Limitation of the Study

The study is important document in context of NPA problem and its solutions in Nepalese financial sectors. Finding of the study might be very much useful for academicians as well as for practitioners. As every study it is also not free from some limitations. It also suffers from following limitations:

- This study is concerned only with non-performing assets of Nepalese commercial banks.
- Only two commercial banks operating in Nepal are considered while study.
- The period of the study is limited from fiscal year 2004/05 to 2008/09.
- The study is basically based on secondary data, articles, publication and journals of the respective banks.

1.7 Organization of the Study

The Research work has been divided into five chapters. They are as follows:

Chapter - I: Introduction

The first chapter includes various aspects of this study like background of the study, focus on the study, statement of problem, objective of study , significance of study and limitation of the study.

Chapter - II: Review of Literature

The second chapter of the study constitutes review of literature. This chapter includes review of books, journal and other relevant Materials such as origin and concept of commercial banks, banking sectors in Nepal and also all relevant information and definition of NPAs

Chapter - III: Research Methodology

The third chapter includes research methodology, which consists of research design, sources of data, population and sample along with different statistical and financial tools used in this study.

Chapter - IV: Data Presentation and Analysis

The fourth chapter includes data and its presentation. These data are analyzed using financial as well as statistical tools to find out some conclusions.

Chapter - V: Summary, Conclusion and Recommendation

The last chapter is Fifth chapter it includes summary, conclusion and recommendation regarding the subject matter.

CHAPTER - II

REVIEW OF LITERATURE

In this chapter, the focus has been made on the review of literature relevant to the non-performing assets and its overall consequences in commercial banks each study is based upon historical data and knowledge, the past knowledge provides foundation to the present study. This chapter helps to take adequate feedback to broaden the information based and inputs to my study, therefore this chapter has its own importance in this study. This chapter is devoted into the conceptual framework, review journals and articles and review of thesis.

2.1 Conceptual Framework

Non-performing assets, also called non-performing loans, are loans on which repayments or interest payments are not being made on time. A loan is an asset for a bank as the interest payments and the repayment of the principal creates a stream of cash flows. It is from the interest payments a bank makes its profits.

Banks usually treat assets as non-performing if they are not serviced for some time. If payments are late for a short time a loan is classified as past due. Once a payment becomes really late the loan classified as non-performing.

A high level of non-performing assets compared to similar lenders may be a sign of problems' may a sudden increase. However, this needs to be looked in the context of the type of lending being done. Some banks lend to higher risk customers than others and therefore tend to have a higher proportion of nonperforming debt, but will make up for this by charging borrowers higher interest rates, increasing spreads. A mortgage lender will almost certainly have

lower non-performing assets than a credit card specialist, but the latter will have higher spreads and may well make a bigger profit on the same assets, even if it eventually has to write off the non- performing loans.
Non-Performing assets (NPAs) could weak bank's profitability both through a loss of interest income and write off the principle loan amount it tackles the subject of in entire starting from the stage of their identification till the recovery of due in such amount (*Bindani; 2003:31*).

To stand with performance in terms of profitability is a benchmark for any business enterprise including the banking industry. However, increasing NPA has a direct impact on banks profitability an legally bank are not allowed to book income on such accounts at the same time banks are forced to make provision on such assets (*Timilsina;1997:46).*

'Nepalese financial institutions have made significant progress during this decade, although they are still far behind the developed markets. In spite of having great risk management i. e. focused on collateral rather than on project, credit culture is a new aspect both to the investors and corporate. Unless we have a credit culture, they will end up nowhere. How to identify a good bank? Hugh deposits, high technology, strong marketing, broad branching network etc? Finally we arrive the point collection of the loans; on the whole, private sector banks have lower non-performing assets NPAs) than their public sector counter parts. NPAs are the loans that cannot be or are not been recovered. The government owned banks suffer actually from this, as they have to lend to various priority sectors, at the whims of their political masters and then forget everything about the money forever (*Baidya;1999:76*).

A bank is judged on the basis of capital, Assets Quality, Management, Easing, Liquidity and sensitivity to market risk (CAMELS). Almost all the government Banks are running at loss. Though almost all the private sectors banks are showing profit, it is very difficult to call them sound if appraised from

CAMELS approach. Some banks have very low capital adequacy ratio (CAR) while some bank have piled up Non-Performing Assets (NPAs). Similarly, banks do not have proper system in place for management of market risks. The people have been raising questions over the correctness of credit classification and provisioning of some banks should the suspicion come true, it will prove very costly to the depositors, creditors and national economy as whole. It would be prudent to advice NRB to strictly implement it's recently introduction directive so that other banks avert the fate of NBL, RBB and NIDC (*Kerlinnger and Wilnston; 1986:24*).

The item 'advance and loan' comes next in the order of liquidity. For all practical purposes, we may say that they are not shift able. Of course, this is the most profitable asset and the profit is mainly derived from these assets. As a rule, a commercial banker will generally lead only for short-term commercial purposes. It is not his duty to provide long-term loans for investment purposes. Such loans are provides by specialized agencies like industrial banks. The reason advanced in support of this view is that in the case long-term loan the banker will find it difficult to realize them when emerges arise. For instance, in the case of a mortgage, the mortgaged properly may cover the loan with a safe margin. But when the bank needs liquid cash most, it may find it difficult to convert the mortgaged property into liquid cash. Here in lays the meaning of the off quoted statement. 'The art of banking' lies in knowing the differences between a mortgage and bill of exchange *(Wolf and Pant; 2002:25).*

The timing of loan repayment is a basic term of bank's lending policy. Loan repayment is generally agreed upon prior to the extension of the loan and should represent a realistic evaluation of the customer's ability to repay. The objective is to secure repayment through liquidation of the transaction being financed by rather than through forced sale of the pledged security. Therefore, term and condition of loan repayment is highly influenced by the nature of transaction type of the loan and the period of loan (*Baidhya; 1999:13*).

Performing assets are those assets loans that repay principal and interest to the bank from the cash flow it generates. Loans and risky assets though a bank invests most of its resources in granting loans and advances. If an individual bank has around 10% non-performing assets/loan (NPAs), it sounds the death knell of that bank ceteris paribus. The objective of sound loan policy is to maintain the financial health of the banks, which results in safety of depositors' money and increase in the returns to the shareholders. Since the loan is risky asset, there is inherent risk in every loan. However, the bank should not take risk above a certain degree irrespective of returns prospect *(Panday; 2000:36).*

Loan review is not a luxury, but a necessity for a sound bank lending program. It not only helps management spot loan-problem more quickly, but also acts as a continuing check on whether loan officers are adhering to the bank's loan policy. For this reason, and to promote objectivity in the loan review process, many of the largest banks separate their loan review personal from the loan department and the bank's board of directors in assessing the bank's overall exposure to risk and its possible need for more capital in the future. Separate loan review division also helps to detect any mishaps and undue influences in the lending process, if any *(Singh; 1999:214).*

2.1.1 Loan and Advances

The major function of commercial banks is to collect deposits or funds and disburse it to investors as loan and advances. This loan and advances are main sources of income. Loan and advances dominate the assets side of balance sheet of any bank. Same way earning from loans and advances occupy a major portion of the income statement of the banks. This asset generates income to the bank. So it also determines profitability of banks. Loan and advances granted to customers earns interest. This interest is major source of income of banks. Loan is granted as overdraft cash credits and direct loans. Banks grant loan on the base of collateral underlying the loan. Banks make careful assessment before granting loans to investors or business enterprises.

2.1.2 Performing Assets/Loans

Performing loans are those loans, which repay principle and interest timely to the bank from the cash flow it generates. In other word, performing loan are the productive assets that generate some profits. Loans have the certain period to return its principle with its interest. If anyone repays loan with its interest on time is known as the performing loan. It is the most profitable assets of bank. Its help in rapid growth of banking sector in this fast pace competitive age. Better performing loan are the symbol of success of bank. It ultimately helps in economic growth and development. So such loans are necessary for overall development and prosperity of country. However, many banks are suffering from the non-repayment of loan amount.

2.1.3 Non-Performing Assets/Loans (NPAs/NPL)

NPAs are defined as bad debt. However, NPA in terms of banking sector consist of those loans and advances, which are not performing well and likely to turn as bad loans. One of the most emerging problems of the commercial banks is to the management of non-performing assets/loans. So banks have to consider and cautious about such loan. While granting loan cautious, careful and through assessment, the project or investor or business enterprises should be made.

"NPA can be defined as the non-productive assets of the banks. In other words, it is the loan or bad debt and doubtful debts that does not repay timely. Generally the loan which does not repay within three months is known as non-performing loan. The loan amount that does not covered by collateral after selling is known as non-banking assets (NBA), Non-performing assets also includes the suspend interest. It is the interest, which becomes receivable.

Unutilized assets and those investments which do not generate any cash or incomes to the bank are also non-performing assets (NPAs). The proper management of those assets to generate income is known as management of non-performing sets"(*Regmi; 2062 B.S. 85:75*). “Meaning of NPAs is different in different country. In some countries, it means that the loan is impaired. In some countries, it means that the payment are due but there are significant different among countries how many days a payment should be in arrears before past due status is triggered” (*Shrestha; 2004:14*). According to current banking act, the banks have to make provision for bad and doubtful debts. After deducting the bad and doubtful debts from the non-performing assets, net non-performing an can be achieved. According to the NRB, central banks NPAs are classified loans and advances according to their nature of overdue timing. NRB has directed to maintain loan loss provision according to aging basis for risk mitigation. The loan provision is to LT be maintained by debiting profit account. Thus as the quality of loan degrades the ratio of loan loss provision is increased affecting the profitability of the banks.

2.1.4 Cause of Occurring NPAs

There are various causes to increase the NPAs. NPAs can be increased due to:

- Wrong choose to project and business to lend the fund
- Lack of transparent and clear lending policy
- Lack of effective and scientific forecast in the actual outcomes of business.
- Lack strong willingness in managerial level of banks.
- Lack of proper legal framework.

2.1.5 Effect of NPAs

Its direct effect is on the profitability of commercial banks. In future, it affects overall performance of banks. It also affects liquidity ad competitive functioning of public and private sector banks and finally the psychology of the bankers in respect to their disposition towards credit delivery and credit expansion.

“Increasing Non-Performing Assets has the direct effects to banks, investors and customers. It has negative impact to the economic health and business of country. It has two types of effects”, (*Batra and Dass; 2003:76*). Internal Effects Profitability is major objective of any business enterprises and commercial banks are not exceptional. But commercial banks cannot mobilize the non-performing assets to increase profitability. They also have to make provision for doubtful debts from their profits and other resources. That's why the profit of banks decreased and may occur losses. As a result, share capital also becomes capital erosion and capital inadequacy. The central bank can take action on those banks, which have low capital or capital adequacy ratio. When the non-performing assets increase, the banks have to increase the amount of provision for doubtful debts and when the loan is repaid, the profit treated as profit. If the provision for doubtful debts crosses 5% of the total loan amount, the bank have to pay income tax as profit. So, it has direct effects to the cash flow of banks'. As a result, the employment of human resources and profit of the bank has also affected.

A) External Effects

The banks accept deposits from the public and provide loan to the operation of business and other purposes. When the loan does not return with interest, it becomes non-performing assets and banks will not be able to return the deposited amount to their customers. If the banks unable to return the deposited amount the banks are loosed public supports and faiths. Not only that much but also. The banks have to take loan at a higher rate to pay deposit, which directly affects the profitability of banks and which leads the bank bankruptcy and dissolve. It also affects the monetary system and economy of the country.

B) Impact on Profitability

The NPAs has negative impacts on the profitability of the bank. Non-performing assets are the idle assets of the banks, which do not generate any return for the banks. Thus, we can say that the NPAs reduce the profitability of the banks due to the becoming the idle resources. Not only has it reduced the profitability of the banks bur also it may causes for losing the customer's faiths and supports.

C) Impact on the Outlook of Banker Towards Credit Delivery

The psychology of the banks today is to insulate them with zero percent risk and turn lukewarm to fresh credit. This has affected adversely credit growth compared to growth of deposits, resulting a low C/D ratio around 50% to 54% for the industry. It is evident that the existence of collateral security at best may convert the credit extended to productive sectors into an investment against real estate, but will not prevent the account turning into NPA. Further blocked assets and real estate represent the most illiquid security and NPA in such advances has the tendency to persist for a long duration. Nationalized banks have reached a dead-end of the tunnel and their future prosperity depends on an urgent solution of this hovering threat.

D) Excessive Focus on Credit Risk Management

The most important business implication of the NPAs is that it leads to the credit risk management assuming priority over other aspects of bank's functioning. The bank's whole machinery would thus be pre-occupied with recovery procedures rather than concentrating on expanding business. A bank with high level of NPAs would be forced to incur carrying costs on a non-income yielding assets. Other consequence would be reduction in interest income, high level of provisioning, stress on profitability and capital adequacy, gradual decline in ability to meet steady increase in cost, increased pressure on net interest margin (NIM) thereby reducing competitiveness, steady erosion of capital resources and increased difficulty in augmenting capital resources. The lesser-appreciated implications are reputation risks arising out of greater disclosures on quantum and movement of NPAs, provisions etc. the non-quantifiable implications can be psychological like 'play safe' attitude and risk aversion, lower morale and disinclination to take decisions at all levels of staff in the banks.

Two decades of regimented and directed banking to credit delivery has deprived bank managers of the instinct skill and knowledge. Nationalized banking did not produce a spring of talent resources. Directive inputs and course direction came externally from NRB and Finance Ministry, which were external to the day-to day affairs and problems of the Nepalese banking industry. The system did not promote initiative and talent, but bred corruption and nepotism. This is the sense of Nepalese Banking struggling hard to transaction from old primitive systems and values to modern professional business ethics and corporate good governance.

E) High Cost of Fund Due to NPAs

Quite often genuine borrowers face the difficulties in raising funds from banks due to mounting NPAs.' Either the bank is reluctant in providing the requisites funds to the genuine borrowers or if the funds are provided, come at a very high cost to compensate the lender's losses caused due to high level of NPAs. Therefore, quite often corporate prefer to raise funds through commercial papers(CPS) where the interest rate on working capital charged by banks in higher. There are other various pressing factors that are relevant from the point of view Nepalese banking operations with a view to focusing on NPAs and its related effects:

F) Excess Liquidity Lending Default

The banks in Nepal are faced with the problem of increasing liquidity in the System 'Further, the Rastriya Banijya Bank (RBB) is increasing liquidity in the system through various rate cuts. Banks can get rid of its excess liquidity by increasing its lending but, often shy away from such an option due to the high risk of default In order to promote certain norms for healthy banking practices, most of the developed economies require all banks to maintain minimum liquid and cash reserves broadly classified into cash Reserve Ratio (CRR) and the Statutory Liquidity Ratio (SLR). A rate cut (for instance, decrease in RR) result into lesser funds to be locked up in NRB's vaults and further infuses greater funds into a system. However almost all the banks are facing the problem of bad loans, nonperforming? Assets, thinning margins, etc, as result of which, banks are little reluctant in granting loans to corporate. As such, though in its monetary policy NRB announces the bankers no longer warmly greet rate cut but such news.

2.1.6 Loan Loss Provision

Risk exists if there are two or more than two outcomes. There is risk in every loan. Loan loss provision is the accumulated fund that is divided as safeguard to cover possible losses. It means that it is accumulated provisioning fund, which is used as safety fund to cover future losses. It is the expected provision fund. The amount of required for provisioning depends upon the level of NPAs, trends of repayment of loan and economic stage of country. The high quality loan requires low loss provision, whereas bad loan requires high loan loss provision. Loan loss provision made for performing loan is called "general loan loss provision" and loan loss provision made for non-performing loan is called specific loan loss provisioning".

2.1.7 Principles of Lending Loan and Advances

The precautions to be taken by a banker, and the principles to be taken care of, While granting advances. By way of introduction, an attempt is being made in the following paragraphs to discuss the general principle to be in mind by a banker while grating advances (*Shekher and Shekher; 1999:551*).

A) Liquidity

The term 'liquidity' implies the ability to produce cash on demand. A bank mainly utilizes its deposits for the purpose of granting advances. These deposits are repayable on demand or on the expiry of a specified period. In either case, the banker must be ready to meet these liabilities whenever necessary. The advances granted by the banker are as liquid as possible.

B) Profitability

Banks are essentially commercial ventures. It is true that excessive and unjustifiable profits can only be at the cost of the customers, in so far higher lending rates push up production costs, and in the ultimate analysis, adversely affects society in general. At the same time, the facts remain that while strong operation profits allow for full prudential provisioning high net profits allow for allocation to capital and reserves, which is essential for any bank to maintain its competitive viability and expand its lending operations. Also, the shareholders of banks are entitled to reasonable dividend. All this indicates that it is that their lending operations are sufficiently profitable.

C) Safety and Security

The banker should ensure that the borrower has the ability and will to repay Advances as per agreement. The banker should carefully consider the margin of Safety. If it is as unsecured advance, it repayment depends on the creditworthiness of the borrower, and that of guarantor. The banker should consider the Charter, Capacity and Capital or reliability, Responsibility and resources of the borrower and the guarantor.

D) Purposes

The banker has to carefully examine applied. Of course the exact purpose the purpose for which the advance has been for which the advance is actually utilized. There is always the possibility that the advances, once granted, may be diverted for purpose so that indicated by the borrower at the time application. Thus there should be proper analysis of purpose.

E) Social Responsibility

While admitting that banker are essentially commercial venture, a bank should not forget the fact that it is not enough that only people of means are given banks finance. The identification of property sectors for the purpose of extending bank credit should be considered as a positive development in the banking system, aimed at effectively discharging its responsibility towards society. At the same time, this social responsibility should not deter the banks from paying adequate attention to the qualitative aspects of lending. Social responsibility is, no doubt ,highly exacting.

2.2 Review of NRB Directives

NRB issues various directives relating banking regulations and prudential norms. Among various directives issued in United Directive 2066 B.S. directive No.2 is relating to loan Classification and provisioning.

Directive No. 2: Loan Classification and Provisioning

Nepal Rastra Bank act, 2058 B. S., granted the central bank full independence in the pursuit of its mandate .It is the duty if independent central bank to be transparent and to communicate. Nepal Rastra Bank's act 2058 B.S. mentioned its role at preamble" whereas, it is expedient to established a Nepal Rastra Bank to function as the central bank to formulate necessary monetary and foreign exchange policies, to maintain the stability of price, to consolidate balance of payment for sustainable development of the economy of the kingdom of Nepal, and to develop a secure, healthy and efficient system of payment, to appropriately regulate, inspect and supervise I order to maintain the stability and healthy development of banking and financial system, and for the enhancement of public credibility towards the entire banking and financial system of country."To fulfill the theme that mentioned on its preamble of act, 2058 B.S. the act 2058 B.S. Chapter 2 sections 4 defined the objectives of Nepal Rastra Banks. Objectives (d) and (e) are related to manage bank and financial system, which are as follows:

a. To regulate, inspect, supervise and monitor the banking system

b. To promote the entire banking and financial system of the kingdom of Nepal and to enhance its public credibility.

To fulfill objectives as a central bank Nepal Rastra bank issue various directives. Banking business is changing day by day not only from the external element but Also within the banks. It is also observed from different element of the society that banking in Nepal is not being operated in such a manner to deserve sufficient public confidence. It is also not operated with due consideration of its long term financial health. This environment in banking business is not only the challenge to the individual bank but also became big challenge to banking and financial as whole and more to the central bank of the country. In order to safe guard from future damage on the banking sector and to have health competition with the banking sector, new directives on code of ethics may help a lot this banking industry.

Directives related to loan classification and provisioning (United Directive No.2) effective from FY 2066/67 B.S., banks shall classify outstanding loan and advance on the basis of aging of principal amount into the following 4 categories.

1) Pass

Loans and advances whose principal amount is not past due for period up to three months shall be included in this category. These are classified and defined as performing loans.

2) Sub-Standard

All loans and advances that are past due for a period of 3 months to 6 months shall include in this category.

3) Doubtful

All the loans and advances which are past due for a period of 6 months to 1 year will be included in this category.

4) Loss

All loans and advances, which are past due for one year or a period of more than 1 year as well as advances which have least possibility of recovery or considered unrecoverable and those having thin possibility of even partial recovery I future shall be included in this category. Loans and advances failing in the category of sub-standard, Doubtful, and loss are classified and defined as Non-performing Loan.

Directive No. 2(a): Additional Arrangement in Respect of “Pass” Loan

Loan and Advances fully secured by bullions, fixed deposit receipts and Government of Nepal securities shall be included under "Pass" category. However, where collateral of fixed deposit receipt or Government of Nepal Securities or NRB Bonds is placed as security against loan for other purposes, such a loan has to be classified on the basis of ageing loan against FDRs of other banks shall also qualify for inclusion under Pass Loan.

The respective overdue period of pass, sub-standard and doubtful loans will be considered for higher classification from the next day of date of expiry of the overdue period provided for each class.

Directive No. 2. (b): Additional Arrangement in Respect of “Loss” Loan

Even if the loan is not past due, loans having any or all of the following discrepancies shall be classified as “loss".

a. No security at all or security that is not in accordance with the borrower's agreement with the bank.
b. The borrower has been declared bankrupt.
c. The borrower is absconding or cannot be found
d. Purchased or discounted bills are not realized within 90 days from the due date.
e. The credit has not been used for the purpose originally intended.

f. Owing to non-recovery, initiation as to auctioning of the collateral has Passed six months and if there convey process is under litigation.
g. Loans provided to the borrowers included in the blacklist and where the credit information bureau blacklists the borrower.

Note

Bills purchased/ discounted are to be classified in to loss loan where they are not realized within 90 days from due date. This is departure from the normal Classification rules applicable to other loans. Accordingly, it bills would have only two classification viz. Pass and Loss.

Directive No. 2 (c): Additional Agreement in Respect of "Term" Loan

In respect of term loans, the classification shall be made against the entire outstanding loan on the basis of the past due period of overdue installment

Loan Loss Provision

The loan loss provisioning, on the basis of the outstanding loan and advances and bills purchases classified as per this directives, shall be provided as follow:

Table 2.1

Loan Loss Provision

S.N	Classification of Loan	Period Beyond Prescribed Limit	Loan Loss Provision
1	Pass	Not Matured or crossed only 3 month after maturity	1%
2	Sub-Standard	Crossed 3-6 months after Maturity	25%
3	Doubtful	Crossed 6-12 months after Maturity	50%
4	Loss	Crossed 1 year after maturity	100%

Source: NRB Directives No. 2

Loan Loss provision set aside for Performing Loan is defined as "General Loan Loss Provision" and Loan loss provision set aside for non performing loan is defined as" specific Loan Loss Provision".

Where the banks provide for loan loss provisioning in excess of the proportional required under the directives of NRB, the whole amount of such additional provisioning may be included in General Loan Provision under the supplementary capital.

Directive No. 2 (d): Additional Provisioning in the case of Personal Guarantee Loan

Where the loan is extended only against personal guarantee a statement of the assets, equivalent to the personal guarantee a mount not claimable by any other shall be obtained. Such loans shall be classified as per above and where the loans fall under the category of pass, sub-standard and doubtful, in additional to the normal loan loss provision applicable for the category, an additional provision by 20% point shall be provided. Classification of such loan advances shall be prepared separately. Hence, the loan loss provision required against the personal guarantee loan will be 21%, 45 and 70%, for pass, substandard and doubtful category respectively.

Directive No. 2 (e): Rescheduling and Restructuring of Loan

In respect of loans and advances failing under the category of substandard, Doubtful or loss, banks may reschedule or restructure such loans only upon receipt of a written plan of faction from the borrower citing the following reason:

a. The internal and external causes contributing to deterioration of the quality of loan.
b. The reduced degree of risk inherent to the borrower/enterprise determined by analyzing its balance sheet and profit and loss account in order to estimate recent cash lows and of project future ones, in addition to

estimate recent cash flows and to project future ones, in addition to assessing market conditions.

c. Evidence of existing of adequate loan documentation
d. An evaluation of the borrower/enterprise’s management with particular emphasis on efficiency, commitment and high standards of business ethics.

Directive No. 2 (f): Loan Loss Provisioning in Respect of Rescheduled, Restructured or Swapped Loan

a. Except for priority sector, in respect of all types of reschedule or restructured or swapped loan, if such credit falls under pass category according to NRB directives, loan loss provisioning shall be provided at minimum 12.5%
b. In case of rescheduling or restructuring or swapping of insured or guaranteed priority sector credit, the loan loss provisioning shall be provided at one fourth of the percentage mentioned in clause (a).
c. In respect of swapped loans, the bank accepting the loans in swapping has to provide loan loss provision classifying the loans under the same classification as were existing. The bank accepting the loan in swapping shall obtain certification from the concerned bank of financial institutions as to the existing classification.

Directive No. 2 (g): Provisioning Against Priority Sector Credit

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

Table 2.2

Provisioning Against Priority Sector Credit

Pass	0.25%
Sub standard	5.00%

Doubtful	12.5%
Loss	25.00%

Source: NRB Directive No. 2

In case of rescheduling, restructuring or swapping of insured or guaranteed priority sector credit, the proportion of loan loss provision would be 3.125% (Being 25% of 12.5%).

Non Performing Asset means an asset or account of borrower, which has been classified by a bank or financial institution as sub-standard, doubtful or loss asset, in accordance with the directions or guidelines relating to asset classification issued by RBI. An amount due under any credit facility is treated as "past due" when it has not been paid within 30 days from the due date. Due to the improvement in the payment and settlement systems, recovery climate, up gradation of technology in the banking system, etc., it was decided to dispense with 'past due' concept, with effect from March 31, 200I. Accordingly, as from that date, a Non performing asset (NPA) would be an advance where:

a. Interest and/ or installment of principal remain overdue for a period of more than 180 days in respect of a Term Loan.
b. The account remains 'out of order' for a period of more than 180 days, in respect of an overdraft cash Credit (OD/CC).
c. The bill remains overdue for a period of more than 180 days in the case of bills purchased and discounted.
d. Interest and/ or installment of principal remains overdue for two harvest seasons but for a period not exceeding two half years in the case of an advance granted for agricultural purpose ,and
e. Any amount to be received remains overdue for a period of more than 180 days in respect of other accounts.

With a view to moving towards international best practice and to ensure greater transparency, it has been decided to adopt the '90 days overdue' norm for identification of NPAs, form the year ending March 31,2004. Accordingly, with effect from March 31, 2004, a non-performing asset (NPA) shall be a loan or an advance where:

a. Interest and /or installment of principal remain overdue for a period of more than 90 days in respect of a Term Loan,
b. The account remains 'out of order' for a period of more than 90 days, in respect of an overdraft cash Credit (OD/CC),
c. The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted,
d. Interest and/ or installment of principal remains overdue for two harvest seasons but for a period not exceeding two half years in the case of an advance granted for agricultural purpose, and
e. Any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

2.3 Review of Journals and Articles

Rajda, (1998) in his article "*Bank Accounting Rule FASB 144 and Loan Loss Provision*?" express that non-performing loans and interest bring the very bad and crucial situations in the banks and it may lead to the bankruptcy.

The market value accounting controversy is not only contentious issue surrounding how bankers keep their books. Another controversy has centered on how banks until recently dealt with the interest income they were losing when customers stopped paying on their loans. Realizing that the industry was for the most part ignoring this issue, the US financial Accounting Standard board recently issued yet another important bank accounting rule, known as FASB 144.

Under this new rule, banks and other financial institutions must account for the expected loss of interest income on non-performing loans when calculating their loan-loss provisions. Many banks still base their loan, not including the expected loss or delay in receiving interest payments. A similar problem arises when the term of the loan must be renegotiated to a longer payout schedule or the bank agrees to reduce or delay interest payments because the borrower cannot successfully handle the originally negotiated term of the loan. Currently, many banks do not report lost interest of they expect eventual repayment of the entire principal of a troubled loan. Statement 144 requires bank to reduce the value of a loan on their books in order to reflect any reduction in expected interest payment as well as any loss of principal. While both secured and unsecured loan are covered, certain loans (such as credit cards and home mortgages) are exempt.

When the adjustment for loss of interest is made, the result is likely to be an increase in loan-loss provisions at those banks not already recognizing interest losses on their non-performing loan. In figuring the value of impaired loans, banks are required by the new FASB rules to measure the value other banks loans by the present value of their expected future cash flows discounted at the loans' effective interest rate (which is the contractual loan rate adjusted fee any deferred loan fee, cost, premiums, or discounts that prevailed when the loan was extended or acquired). Each quarter bankers must estimate when their troubled loans are likely to be repaid, if ever.

Pakuryal, (2001) has stated in his articles entitled' "*Our Economy is in a Volatile Stage'* that the banks have not able to collect their overdue to the increasing cumulative NPAs in Nepalese commercial banks' there is no additional demand of the investments due to the higher risk and present uncertainty.

According to him, "revenue collection is negative and regular expenditure is higher than the revenue. This indicates volatility of the economy. Even before the declaration of emergency; the government did not have surplus revenue to pay for the remuneration and benefits of retired civil servants. The year 2002 is going to be difficult as major loans are going to mature. Debt servicing will also demand a significant share of the budget. Up to 65% of our development, expenditure is being financed by foreign aid. However, if we can't meet the regular expenditure (through our revenue), it will be very difficult for us to convince the donor community. This could push our society toward what is called a ’mass unrest society”.

He also adds, “The government is about to establish as Assets Management Company to take over the non-performing assets (NPAs) of the government owned banks. On the other hand, it looks like the government's entire concentration has been on two commercial banks only (Nepal Bank Ltd. and Rastriya Banijya Banks). Due to cumulative growth of the NPAs, the banks haven't been able to collect their overdue. Due to the present uncertainty and higher risks; there is virtually no demand for new investments. That's why many banks are concentrating on conventional areas. We haven't been able to explore potential areas of competitive advantage in the regional context" After 1990, we have seen that macroeconomic stability could not ensure the reduction of poverty. If the present rate of economic growth and population growth continues, it will take at least 20 years to double our per capita income. It has been proved that macroeconomic stability alone can't ensure economic development in a country like Nepal. At the same time, the low-level of inflation at present may not reflect future prospects for Nepalese economy.

Upreti, (2001) in his article titled “*More on Blacklisting*" suggested that "it can be gathered from the published materials that the funding agencies are pressuring the NRB to clean up the nonperforming Assets (NPAs) from the balance-sheets of some government owned banks and financial institutions as a part of the effort of reforming Nepali financial system, where as being the prime regulator and custodian of Nepalese economy.NRB should have been acting on its own. The NRB may well have found a shortcut to that goal in the form of the Directive. However, in doing so, the leadership of NRB is forgetting that it is cutting the same branch of a tree on which it is sitting. Moreover, the Directive fails to address the real problems that are giving rise to accumulation of such huge NPAs. The major contributors to the huge NPA are the government owned banks whose lending are political lending and corrupt lending (with the involvement of security valuators and managers of the banks),where the management is unaccountable and inefficient. This is also the result of waiver of prudential norms granted to these pampered government banks in the past on case basis. Unfortunately, the directive, following this tradition, still exempts the directors of the government owned corporate bodies from its ambit."

He concludes, the contents of the directive also suggest that the NRB is lacking a leadership which has dynamism and is capable of using prudence. In decision making on matters having long term impact on the overall economy of the nation. Such dynamism and capability was expected from the new autonomous Rastra Bank as envisaged by the Nepal Rastra Bank Act 2058.The expectation has been belied.

Chhetri, (2007) in his article "*Non-performing Assets: A Need of Rationalization*" expressed that NPA is hindering gainful investment. He also showed the difference of NPA conceptually in various countries.

Loan and advances of financial institutions are meant to be serviced either part of principle of the interest of the amount borrowed in stipulated time as agreed by the parties at the time of loan settlement. Since the date becomes pat dues, the loans become non-performing asset. The book of the account with lending institution should be effectively operative by means of real transaction effected on the part of the debtor in order to remain loan performing.

The definition of NPA differs from country to country. In some countries of Asia Pacific Economic Cooperation (APEC) forum, a loan is classified as non-performing only after it has been arrear for at least 6 months; similarly, it is after three months in India. Loans thus defaulted are classified into different categories having their differing implication on the assets management of financial institution opined by him. NPAs are classified according to international practice into three categories namely substandard, doubtful and loss depending upon the temporal position of loan default. "Thus the degree of NPA assets depends solely on the length of time the assets has been in the form of none obliged by the loan. The more time it has elapsed the worsted condition of assets is being perceived and such assets are treated according" stated by him.

Chhetri's view, failure of business for which loan was used, defective and below standard credit appraisal system, credit program sponsored by Government, slowdown in economy/recession, diversion of fund is some of the lending to accumulation of NPAs.

There is serious implication of NPAs, on financial institution. He further adds that the liability of credit institution does not limit to the amount declared as NPA but extend to extra amount that requires by regulation of supervisory authority in the form of provisioning as the amount required for provisioning depends upon the level of NPAs and their quality.' His view is rising level of NPAs create a psyche of worse environment especially in the financial institution like waiving interest, rescheduling the loan, writing off the loan 'appointing private recovery agent, taking help of tribunals and law of land etc' NPA can be reduced. Finally, he concludes that financial institutions are best with the burden of mounting level of NPAs in developing countries."' Such assets debar the income flow of the financial institution while claiming additional resources in the form of provisioning thereby hindering gainful investment' Rising level of NPAs cannot be taken as stimulus but the vigilance demanded to solve the problem like this , eventually will generate vigor to gear up the banking and financial activities in more active way contributing to energizing growth warned by him.

Neupane, (2001) expressed in his article titled *'NPAs at Nepalese Financial Institutions'* ,that the thinking rationally no one shall be surprised to note two of the giant commercial banks of this country such as Nepal Bank Ltd and Rastriya Banijya Bank accounting for the highest number and amount of non-performing assets(NPA) among players in the industry. In general and more specifically, in least developed countries like ours, the larger the size of the credit portfolio the larger the amount of NPAs.

He further states, "The concept and realization of NPAs in the Nepalese financial sector revolved round about a decade ago along with the notion of prudential accounting norms. I reckon that ten years timeframe should have been more than enough to formulate and implement strategies for identifying an analyzing the ever accumulating NPAs are Nepalese financial institutions (FIs). However, the Nepal Rastra Banks (NRB seems to have realized the panic only a year ago. As a result, the NRB came up with a nineteen-point strategy, primarily pertaining to ways to tackle NPAs. Some of the measures the NRB has envisaged are formation of an assets reconstruction company, credit rating agencies, legal reforms, strengthening administrative/monitoring/supervising mechanisms etc. and above all, the recent NRB directives (1 to 7). Although the NRB, vies-a-vies the FIs would have been much better off had it come up with all these philosophies some five years ago, better late than never?."

He expressed the one major that can be attributed for the already prevalent and ever increasing NPAs is unhealthy competition among the commercial banks. Since, the size of our economy has remained more or less stagnant over the past half a decade or so, the size of the total i.e. has not changed much. Every player in the market mean business and its primary motto is 'making profit". This has enhanced unhealthy competition among the banks through interest rate reduction, issuing loans irrespective of borrowers' credibility and authenticity, etc. In course of making their credit portfolios bugger, all the players have been pouring their investments into the same pie thereby over financing the pie.

Given this scenario, it is no surprise to discover a good loan turning into NPAs because of over financing.

There is no denying that no capital market around the world can be termed perfect' However, the capital markets are primarily driven by certain norms, which make loss of sense, and every single movement including stock price fluctuation is surprisingly, share by prudential norms. By contrast, share prices at NEPSE are bound to move upward if a bank registers say Rs 800 million in profit, an accounting profit, even if it does not contribute accumulating a sizable NPA, a manage to fool the generate public in terms of the accounting profit it registers.

Even the most profitable sector of the economy, be it a primary source of foreign currency earning, should not be over financed. There should always be an upper limit for any sector that deserves bank financing. Recently, the NRB came up with a directive to lessen risk concentration on a single borrower/single sector of the economy. The directive states that large sectoral concentration constitute a source of risk. Bank management shall have adequate internal policies and systems in place to monitor the bank’s sectoral exposure. However, if the NRB so directs, judging it necessary, a bank shall have to provide additional capital with a view to providing uniformity in the categorization of various sectors of the economy,' NRB's policy of limiting FIs from pouring their lending into a single sector of the economy can be regarded very positive since it is likely to diversify the risk of the total investment evenly and there by minimize the risk of NPA.NRB shall continue to be more stringent in formulating firm policies in the days ahead too to protect shareholder interests.

At last, even if the banks endeavor to recoup NPAs through the auction of Mortgaged property, the legal system and the regulations are so shabby and Defaulter friendly that they have to struggle for many years to realize the auction Process. Just imagine this process, a borrower initially, defaults payment, the banks calls back the loan, six months there on the concerned authority blacklist the borrower, a 35 days' notice goes to the papers for auction and after that a 7 days ultimatum and so on and so forth. Hundreds of cases have been lingering in the courts for many years. In efficient legal provisions, from the point of view of the bankers, have encouraged borrowers to default and contributed more towards enhancing the quantum of NPA in Nepalese FIs.

Dhungana, (2001) in his article titled "*NPA at Nepalese Financial Institution*" has tried to highlight one of the approach mainly Assets Management Company (AMC) for resolving the problem of NPL. As per him, AMS is the specialized financial intermediary to manage the non-performing and distress loans of banks and financial instructions who buy the NPL from financial institution and take necessary steps to recover the maximum value from the acquired assets. As per his view, if NPLs are not resolved in time there would be inherent direct to indirect costs to the economy. As stated by him NPL may arise due to the external factors like decrease in market value of collateral deterioration borrower's repayment capacity, economics allow down, borrower's misconduct, improper credit appraisal system, lack of risk management practice, ineffective credit monitoring and supervision system. Hence he suggested that, NPL should be kept at minimum level and the specialized institution such as AMCs should manage the distressed loans.

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

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

Joshi, (2004) in his article titled "*RBB Reducing Losses*", The New management team has broken its silence after nearly 11 months of taking the management to the bank in its hand. And the team revealed at a press conference held in the middle of December, the annual operating loss of the bank has been reduced to Rs. 730 million in the fiscal year 2002-03 as compared to Rs.1230 million in 2001-02. Joshi, sounded jubilant announcing that the annual operating loss is projected to come down to mere Rs. 20 million in the current fiscal year that is ending in mid-July 2004.

Most interest information revealed by RBB senior executives on that occasions perhaps regarding the reduction in NPA. During the nine months, the banks recovered Rs.2300 million as principal and interest from the loans that were classified as NPA. Sounds Fantastic? But RBB executives say it is not that fantastic reason? Not all of the NPA was really bad. The money was not being recovered in the past just because there was no follow up made on the loan to realize it. The culture seemed to be that of "lend and forget". More importantly, the NPA size has gone up from Rs.14889 million as of Mid-July 2002 to Rs. 15531million as of mid-October2 003.But RBB executive say it was due to the more stringent requirements introduced recently under the prudential directives of Nepal Rastra Bank". The article titled "Options *for the Failed Banks*" was published in New Business age in economic and policy "the resolution of non-performing loans (NPLs). Whether the NPLs should remain on the books of the two banks, or be transferred to an asset management company, and the arrangement for the accelerating and maximizing recovery, are matters, which may be negotiated with potential buyers, at the time of sale. Removing the NPLs is likely to attract a better price for the two banks, but at a cost to Government of Nepal of the interest on bonds paid in compensation. The buyer would own a fully capitalized bank in this case, since the existing loan loss reserves could be reversed, once all NPLs were removed. However, some potential buyers which pride themselves in their asset management skills might be prepared to buy the two banks with the NPLs included, if the NPLs are fairly priced. Whether, the buyers accept the NPLs or not, they may be willing to act as agent for securing recoveries. The amount of NPLs for consideration will be determined after qualified potential buyers have completed their due diligence.

Sapkota, (2004) in his article titled "*Portion of NPA in Commercial Banks-Highly in public, Low in private*" has written which was published in Rajdhani on 19'h May 2004. in his article, he has stated that the problem of NPL is seen less in private banks in comparison to Public banks. The NPA of two big nationalized banks being about 60% if the total loans are very serious situation. He further mentioned that in order to improve this situation and to make healthy banking environment, financial reform program has been brought as its consequences, the management of two big banks was handed to foreign company on a contract but he ratio of NPL was not reduced.

Even most of the private owned banks has NPAs within international standard, privately owned bank's NPA is higher that international standard. As per standard 5 % NPA is acceptable. He also states that, Nepal's total NPA of banking sector is 30% which is very high.

Tiwari, (2006) expressed in his article titled “*Budget 2006-07: A Long Way Go*” that Nepal's financial sector seems to be swimming troubled waters for sometimes now. "The major problem stalking the Nepali banking sector is non-performing assets (NPAs) that stand close to a staggering Rs. 29 billion as a whole, which is above all attributed, to slow implementation of policies and directives issued by both the government and the Nepal Rastra Bank (NRB). Of the total banking sector's loans worth Rs 159796 million to different sectors so far, 18.19 percent goes under non-performing loans, according to NRB sources. Nepal Bank Ltd (NBL) and Rastriya Banijya Bank (RBB) occupy the lion's share in these NPLs. As per international norms, NPA level should be maintained below five percent. But NBL and RBB have NPAs far in excess of this. RBB recently has reduced its NPAs to 50% from its earlier 57%. Similarly, NPAs at NBL run into 43%.If this Rs 29 billion in NPL is not recovered, it would obstruct all economic activities in the economy."The writer suggests that the absence of an Asset Management Company (AMC) has not helped in the battle against NPAs. The Dr Shanker Sharma Task Force had recommended strong steps to reform the banking sector, but they could not be implemented.

Mundat, (2006) expressed in his article titled "*Banks cut NPAs to global levels*" that the dead weight of non-performing assets (NPA) on the banking industry, which at one time threatened to bring down a few banks, has significantly reduced. The strong momentum in economy and cleansing of balance sheets through provisioning has brought down bad loans in Indian banks to globally acceptable levels. Today; Indian banks have NPA ratios that are largely in line with their global peers.

Golchha, (2007) in his article "*NPAs at Nepalese Financial Sector* " has highlighted NPA problem in Nepalese financial sector. In his view "the NPAs of the three banks (NBL, RBB and NIDC) are highly discussed and published. If we analyze them, we can find that the NPA of these banks have also made the required loan loss provisioning over the same period, high and improbable figures of NPA are still often quoted. There are many companies, which suspended their business one or two decade ago, but the banks are still carrying their loan account as NPA in their looks. They should have the guts to either foreclose on the collateral or write the loan off in such cases."

Neupane, (2008) in his article titled "*Banks Cut NPAs to Global Level*" has thrown some views regard bad loans of banking sector. As mentioned by him there was various type of risk inherent in the credit. One, who managed risk, earns profit. He further added that recent financial crisis in banking sector is due to weak accounting procedures, defect in loan classification, lack of transparency, loss control measure etc.

He opined that NPL is the indicator of financial crisis and the factor leading to NPLs is economics low down, recessions, bad intention of the borrower, lack of credit policy, increase in interest rate etc. NPLs increases resource mobilization cost and reduces profit-earning capacity of the bank. He has also mentioned that the international standard of acceptable NPA is 40% but here is about 26% NPL in Nepalese banking sector, which is due to high level of NPL of two nationalized banks. As stated by the writer, the major implications of NPL are banks cannot return depositors money on demand and it limits lending capacity of the bank. The writer suggested internal and external measure for reducing NPL and its effect.

Internal measures comprise classification of loan and advances and providing provision for probable loss and external measure comprises to help from credit Information Bureau (CIB), appointment of Asset Management Company (AMC) and Debt Recovery Tribunal (DRT).

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

Ghimire, (2008) in his article titled "*Credit Sector Reform and NRB*" has tried to highlight the effects of change or amendment in NRB directives regarding loan classification of loan loss provisioning." Although the circumstances leading to financial problem or crisis in many Nepali banks differ in many respects, what is a common are most of the bank is the increased size of non-performing-assets (NPAs).To resolve the problem of the loan losses or likely losses of this nature facing the industry NRB has as the central bank amended several directives and issued many new circulars in the recent years"

As opined by him, since majority of the loans of most of the commercial banks of the country at present falls under substandard, doubtful and even loss categories, loan loss provisioning now compared to provision arrangement would be dramatically higher. The new classification and provisioning norms are very last as they help to strengthen banks financially. He added that we also must remember that the old system remained in force from 1991 to 2001, which was probably the most volatile decade of the business operation of the country. He has indicated that loans loss provisioning as a percentage of total credit of April 12.2001 is 5.2% but as April 13,2003,it has jumped to 18.39.If only private banks are considered, it is 2.12% of April 200 1where as it is 6.30% as of April 13,2003, The total increment in LLP is Rs 11 328.11 million and the total increment in credit is only Rs 7976.7. He has also stated that tightening provisioning requirements on NPL is essential to ensure that banks remain liquid even during economic downturns.

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

2.4 Review of Related Thesis

Ojha, (2005) in his study "*Lending Practice: A Study on Nabil Bank Limited. Standard Charted Bank Nepal Limited and Himalayan Bank Limited*" his main objectives of the study are to analyze, the various aspects of bank's lending in various sectors of economy, the individual bank's performance regarding the lending quantity, efficiency and its contribution in total income. The problem, conclusion and recommendation figured out by him in this thesis are discussed as below. As stated by him, over liquidity caused due to lack of good lending opportunities, risks arising due to mismanagement of lending portfolio, increasing non-performing assets etc. are some of the problems that is facing by Nepalese banking sector. His main objectives to analyze the various aspects of bank's lending in various sector of economy, the individual bank's performance regarding the lending quantity and quality.

His major findings and conclusions are "The highest growth rate, proportionately high volume of loans and advances' the best contribution in priority and agriculture sector and the high level of deposits mobilization of

HBL has put this bank in the top position in the lending function. However the better activity ratio of SCBNL has proved this bank the best in managing the lending portfolio according to the demand of profit oriented business. The high volume of lending activities and high volume of productive sector loan of NABIL has put the bank in the top position in absolute terms. The increasing provision on loan loss and high volume of non-performing assets in NABIL & HBL certainty attracts the high attention of any person interested with these banks. The high volume of NPA of HBL may have caused due to the failure industrial and agricultural sector. NABIL's increase N PA may have caused due to the accumulated bad debts that is kept behind the certain to show the high efficiency of management".

Maharjan, (2006) in his study "*NRB Directive, Their Implementation and Impact on Commercial Banks: A Case Study of Himalayan Bank Limited*" with the main objectives are: to examine loan loss provision in commercial banks, to evaluation the proposition of non-performing loan and the level of NPAs in total assets, total deposits and total lending in the Nepalese commercial banks, to analyzed the impact of non-performing assets in the performance of commercial banks and to evaluate the relationship between loan and loan loss provision in commercial banks. His has observed that the changes in NRB Directives have made the impact on the commercial banks. Because of new Directives, banks have to increase the operation cost and dividends to shareholders and bonus to the employees are scaled down due to decrease in profits of bank. He has also observed about the protection of deposits of public because of reduction in the loan exposure. He further states that due to new directives, its foresight results lead to banks financially healthy and stronger in future. Finally, he laid down about the changes in directives will bring prosperity to the shareholders, depositors, employees and the economy of the country as a whole. He suggested, in his thesis, to NRB that the "NRB should issued directives after being proper homework. NRB must strengthen the functioning of its credit information Bureau. NRB should be practical and should issue directives to be applicable in the context of Nepal, not only to meet the international standard. Otherwise, complaints from commercial banks may arise. However, in the present context, the commercial banks have to comply such directives and maintain its policies and NRB has directed commercial banks to obey such rules and regulations, otherwise NRB will take action as per RB Act, 2058 B.S.

Presently, NRB has issued directives relating to banking regulations and prudential comprises then directives. The findings of above study may indicate the certain impact of the new directives to the commercial banks."

Shilpakar, (2006) in her study "*A study on Lending Practices of Finance Companies of Nepal*" with the main objective to analyze performance of finance company regarding lending quality and its contribution in profitability. She concluded that Loans and Advances is one of the main sources of Income of finance companies. This is also shown by the high degree positive correlation between total income and Loans and advances. "Loan Loss Provision is like a by-product of loans and Advances thus, with Loans and Advances, Loan Loss Provision does increase in synchronize". She recommended that Loans and Advances of Finance companies are increasing and so are the non-performing loan and loan loss provision. Hence extra efforts should be enforced to control over NPL.

Shrestha, (2007) in his thesis "*A Study of Non-performing Assets of Nepalese Commercial Banks: With reference to NBL, Nabil Bank Limited and SCBL*" with the main objectives are: to examine loan loss provision in commercial banks, to evaluation the proposition of non-performing loan and the level of NPAs in total assets, total deposits and total lending in the Nepalese commercial banks, to analyzed the impact of non-performing assets in the performance of commercial banks and to evaluate the relationship between loan and loan loss provision in commercial banks. She has analyzed NPA position of NBL, the government owned bank. In his thesis, he deemed NPA as major problem of RBB and almost the whole banking sector. According to him Rs 29 billion is staggering as NPA in Nepalese banking sector. Such a huge amount of NPA is due to slow implementation of policies and directives used by both the government and the NRB. Its recovery is immensely important for the economic development of country. Finally he warns that if these NPA are not recovered it would obstruct all economic activities in banking sector of the country.

Ghimire, (2008) in her thesis "*Comparative Study of Non-Performing Loan of Nepalese Commercial Banks: With Reference of Nebil Bank Ltd., Nepal Credit and Commercial Bank Ltd. And Nepal Investment Bank ltd."* has tried to analyze NPA and NBA of commercial banks. Her main objectives are: to evaluate the proposition of non-performing loan and the level of NPAs in total assets, total deposits and total lending in selected banks. She has found out bad intention, weak monitoring and mismanagement are the most responsible factor for NPA growth. Likewise, legal provision for recovery as a reason for increment in NPA in Nepalese Banks has been found the factor having least impact supervision and monitoring system has been identified as average factor. At the same time, it has been identified that commercial banks give highest priority to trade sector for lending its resources. Then it is found that the service sector is not given much priority.

Koirala; (2009) in her study "*A Study on Non-performing Loan in Nepalese Financial Sectors*" with an objective to find out of non-performing loan in selected commercial banks and relationship between loan and loan provision in selected banks, to analyze performance of finance company regarding lending quality and its contribution in profitability, to examine loan loss provision in commercial banks, to evaluation the proposition of non-performing loan and the level of NPAs in total assets, total deposits and total lending in the Nepalese commercial banks He concludes ineffective credit policy, political pressure to lend to unaccredited worthy borrowers, overvaluation of collateral are the major causes of mounting non-performing assets in government owned banks like NBL. Other factors leading to accumulation of NPAs are weak loan sanctioning process, ineffective credit monitoring and supervision system, economic slowdown, borrower's misconduct etc. continual review and to take remedial action to counter deterioration in credit quality. In addition to this establishing recovery cell, hiring Asset Management Company are also measures to resolve the problem of NPLs. The present loan classification and provisioning directive seems more stringent than the previous one. As a result more provision has to be appointed leading to lesser profitability but this kind of negative impact is only for short period. Adequate provisioning strengthen she financial health of the banks and makes them able to face any kind o future contingencies.

From the above analysis mainly the objectives found to be set are: to evaluate the proportion of non-performing loan and level of NPAs in total assets, total deposits and lending in selected banks, to examine whether Nepalese commercial Banks are fulfilling the NRB directives/ regulation regarding loan loss provision for the non–performing assets or not, to present the trend line of the non-performing assets, loan and advances, loan loss provision of selected banks. But it is not studied that what is the impact of non-performing assets in the performance of the commercial banks, what is the relationship between loan and loan loss provision in the commercial banks and what may be the suggestion and recommendation for further improvements in performance of commercial banks?

CHAPTER - III

RESEARCH METHODOLOGY

3.1 Introduction

Research is conducted for various reasons. Good research result is based upon good and well planned research methodology. To accomplish research and find out the objective of research it must be systematically managed. This study aims to evaluate the impact of non-performing assets on various sectors of commercial banks. The objective can be achieved by analyzing the activities i.e. deposit, loan and advances and investment of commercial banks.

In the previous chapter, the conceptual framework regarding non-performing assets and relevant literature has been reviewed so as to broaden the base of this Study. As a result these study and analysis has become a major tool to choose research methodology

Research methodology refers to the various sequential steps to adopt by a researcher in studying a problem with certain objectives in view *(Kothari;1989)* in other words research methodology describes the method, procedures and plans of conducting research. It is a blue print to achieve goal. Appropriate and adequate methodology yields more accurate conclusions and findings which ultimately help to recommend viable solutions to their search problems.

3.2 Research Design

A research design is specification of method and procedures for acquiring the Information needed. It is the plan, structure and strategy of investigation conceived to obtain answers to research questions and to control variances. It is the overall operational pattern of framework of the projects that stipulates what information is to be collected from which sources by what purpose. Good design will ensure that the information obtained is relevant to the research question and that it is collected by objective and economically procedure.

Research design is the plan, structure, and strategy of investigation conceived so as to obtain answers to research questions and to control variance *(Kerlinger; 1986).*

According to Kothari," A research design is the arrangement of conditions for collections for collection and analysis of data in a manner that aims to combine relevance to research purpose with economy in procedure.”

The main objective of research design is to make analysis in non-performing Assets of commercial banks in Nepal and provide valuable recommendation. In other words, this research is aimed at studying the non-performing assets of commercial banks. This will follow analytical and descriptive research design. Hence, this research will be conducted on the base of historical data covering five years' transaction of commercial banks.

3.3 Sources of Data

Basically, there are two types of data one is primary and second is secondary data. These data are classified on the basis of the nature of collection. Primary data: Primary data is collected for the first time and it is original in its form. On the basis of research questions information are directly gathered from the informant is known as primary data. These data are collected from the informant directly. These data are first hand information.

Secondary Data: Secondary data are reused data. Those data already collected by various individuals and organizations in the form of primary data and secondary data are known as secondary data.

This research is based upon secondary data. Secondary data collected from various sources are used to find out various research problems. The study is mainly based upon secondary data. Sources for these secondary data are taken from financial statements of banks. Besides this all relevant information from various sources are referred. Hence for the purpose of research various plans, structure and strategies are designed. To achieve the objective of the study, descriptive and analytical research design has been proposed. Some financial tools and statistical tools may come in use. This study has been conducted on the basis of secondary data. The data related to the research purpose like deposit, investment, loan and advances etc. are obtained from banks, central bank and various publications. The supplementary data are obtained from various institutions and regulatory bodies like Nepal Rastra bank, Security Exchange Board, Ministry of Finance and National Planning etc. All the secondary data are compiled, processed and tabulated in the time series as per t he need and objectives'

3.4 Method of Analysis

Both statistical and financial tools are used in this study. The analysis of data will be done according to pattern of data available. Because of limited time and sources, simple analytical statistical tools such as graph, percentage, Karl Pearson's co-efficient of correlation and the method of least square are adopted in this study. Similarly some strong accounting tools such as ratio analysis and t rend analysis have also been used for financial analysis. The various calculated results obtained through financial, accounting and statistical tools tabulated under different headings. Then they are compared with each other to interpret the results.

3.4.1 Financial Tools

Financial analysis is the process of identifying the financial strength and weakness of the firm by properly establishing relationship between the item of balance sheet and profit and loss account (*Pandey; 2000:108*). while adopting financial tools a ratio is used as benchmark for evaluating the financial position and performance of any firm, "financial analysis is the use of financial statement to analyze a company's financial position and performance and to assess future financial performance (*Wild, Subramania and Halsey; 2003:13*).

Ratio Analysis

Ratio analysis is the most effective tool of financial analysis. It is the widely used tool in financial analysis. A ratio simplify shows the relationship between the two variables or one another. It presents the relative strengths and weakness of any firm or organization. It also shows the financial growth of the organization and financial performances of the organizations. It summaries the financial figures and make quantitative judgment about the financial performances and positions. The relationship between two accounting figures expressed mathematically is known as financial ratio *(Pandey; 2000:108).* To make analysis w e can use various ratios. But only those ratios have been calculated which are related to the research topic.

Loan and Advances to Total Assets Ratio

The loan and advances to total assets ratio measures the amount of loan and Advances in the total assets. It means that it shows the proportion of loan and Advances to total assets. High degree of loan and advances indicates the good position of the organization that of good mobilization of deposits of funds. In inverse, low degree of loan indicates that is no use of fund properly. Loan is the risky assets. Thus, higher loan and advances to total assets ratio shows high risk and inversely low loan and advances to total assets ratio shows low risk. Risk consist the uncertainty and future is uncertain. Thus, the loan and advances may or may not be recovered with its interest. This ratio can be calculated as follows:

Loan and advances to Total Assets Ratio= $\frac{\text{Loan and Advance}}{\text{Total Assets}}$

Loan and Advances to Total Deposit Ratio (CD Ratio)

The loan and advance to total deposit ratio shows the relationship between the loan and advance and total deposit. It shows how much fund of deposit is provided as loan and advance. This ratio is used to find out how successfully the banks are utilizing their deposited fund on credit or loan for profit generating purpose as loans and advances yield high rate of return. Higher CD Ratio implies the better utilization of total deposits and better earning. Hence 70% to 80% CD ratio is considered as more appropriate. This ratio can be calculated as follows:

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

Non-performing Assets to Total Loans and Advances Ratio

This ratio determines the non-performing assets in the total loan and advances portfolio' Greater ratio implies the bad quality of loan of the bank. Hence lower non-performing assets to loans and advances ratio are preferable. As per international standard only 5% NPA is allowed but in the context of Nepal 10% NPA is acceptable. It is calculated as:

NPA to Total Loans and Advances Ratio =$\frac{\text{Non-Performing Assets}}{\text{Total loan and Advances}}$

Provision Held to Non-performing Assets Ratio

This ratio describes the proportion of provision held to non-performing assets of the bank. This ratio measures up to what extent of risk inherent in NPA is covered by the total loan provision. Higher ratio signifies that the banks are safeguarded against future contingencies that may create due to non-performing assets. So,, higher the ratio better is the financial strength of the bank. This is expressed as:

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

Non-Performing Assets to Total Assets

This ratio indicates the ratio between the non-performing assets and total assets. Higher NPA to total assets ratio implies the bad affects in banks performance and it decreases the profitability of the banks and lower ratio implies the better Performance of the bank and it increases the profitability of banks. This ratio can be calculated as follows:

$$\text{NPA to total Assets} = \frac{\text{Non- Performing Assets}}{\text{Total Assets}}$$

Return on Loans and Advances

This ratio indicates the proportion of the return over total loans and advances. It Describe show efficiently the bank has utilized and mobilized its resources in the form of loans and advances of the banks. Higher the ratio better is the performance of the banks and vice versa. It is calculates as:

$$\text{Return on Loan and Advances} = \frac{\text{Net profit}}{\text{Total loan and Advances}}$$

3.4.2 Statistical Tools

The statistical tool is essential to measure the relationship of two or more variable. It is the mathematical technique used to facilitate the analysis and interpretation of the performances of the organizations. It also helps to present the data, show the relation and deviations or differences of variables of organizations. In this study, the following statistical tools are used:

Arithmetic Mean

The arithmetic mean or simple mean of set of observations in the sum of all the observation divided by the number of observations. It is the best value, which Represent to the whole group... means is the arithmetic average of a variable. Arithmetic mean of a series is given by:

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

Where, $\sum X$ =Sum of the variables 'x'

N= No. of Observation

This tool is used to find out mean of Total Deposit, total loan and advances Non- Performing asset, Loan Loss Provision.

Standard Deviation

The standard deviation is the absolute measure of dispersion in which the drawback present in other measure of dispersion as it satisfied most of the requisites of a good measure of dispersion. Standard deviation is defined as the positive square root of the mean as square of the deviation takes from the arithmetic mean. It indicates the ranges and size of deviance from the middle or mean. It measures the absolute dispersion. Higher the standard deviation Higher will be the variability and vice versa.

Dispersion measures the variation of the data from the central value. In other words, it helps to analyze the quality of data regarding its variability. It is calculate as:

Standard Deviation (σ) = $\sqrt{\frac{\sum x^2}{N} - \left(\frac{\sum x}{N}\right)^2}$

This tool is used to calculate the deviation of total deposit, total loan and advances, loan loss provision and non-performing assets.

Co-efficient of Variation (CV)

Standard deviation is the absolute measure of dispersion. The relative measure of dispersing based on the standard deviation is known as the measurement of coefficient of standard deviation. The percentage of measure of co-efficient of so is called co-efficient of variation. Less CV is the more uniformity and consistency and vice versa. Only standard deviation is not appropriate to compare two pairs of variables but also CV is capable to compare two variables independently in terms of their variability. It is calculated as under:

Coefficient of Variation (CV) = $\frac{SD}{Mean} \times 100$

This tool is also used to find out the consistency of total deposit, total loan and advance, loan loss provision and non-performing assets.

Correlation Coefficient (r)

Correlation coefficient is defined as the association between the independent Variable and independent variable. It is a method of determining the relationship between these two variables. If the two variables are so related change in the value of independent variable cause the change in the value of dependent variable then it is said to have correlation coefficient.

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

The Karl Pearson coefficient of Correlation always fails between- 1 to +1. The Value of correlation of coefficient in -1 signifies the negative correlation and in +1 signifies the positive correlation coefficient.

If, r = 0, there is no relationship between the variables

r < 0, there is negative relationship between the variables

r>0, there is positive relationship between the variables

r - 1, the relationship is perfectly negative between the variables

r +1, the relationship is perfectly positive between the variables

The correlation coefficient gives the actual relationships but sometimes it may give the effort. The reliability of the correlation coefficient(r) can be checked with the help of probable error (PE). It is calculated as follow:

Probable Error (PE) = 0.6745 $\times \frac{1-r^2}{\sqrt{N}}$

Where,

r = correlation coefficient

N = no. of Observation

Decision:

If r > 6 PE, the correlation coefficient is significant and reliable

If r < 6PE, the correlation coefficient is insignificant and there is no evidence of correlation.

Correlation coefficient and probable error are statistical tools. These tools are used to find correlation between loan loss provision and non-performing asset between loan and advances and total deposit and between loan loss provision and loan and advances.

Trend Analysis

A series formed from asset of statistical data arranged in accordance with their Time of occurrence is said to be a time series. It is one of the statistical tools, which indicates the improvement or decrement of the financial situation. It helps to determine the future values of the variables. The way from which the maximum information can be drawn from the figure collected is known as the analysis of time series.

Y = a+ bx

Where,

Y = trend value or dependent variables

a = Y intercept

b = Slope of trend line of the amount of change in Y variables that is an associate with change in 1 unit in X variable

x =Time variable

This is also very important statistical tools. This tool is used to forecast loan and advances, loan loss provision and non-performing assets and also net profit of the company.

Graphical Representation

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

CHAPTER-IV
DATA PRESENTATION AND ANALYSIS

4.1 Ratio

4.1.1 Loan and Advances to Total Deposit Ratio

Loan and Advance is major function of commercial banks. Its circulation plays vital role in the profit of company and its overall performance of company. Banks must be able to use its fund and assets as loan and advances.

Same way deposit collection is major function of commercial banks. These deposit demands interest. Collected deposits in the form of saving and fixed deposits are to be paid certain interest. So, if banks are unable to mobilize these deposits in the form of loan and advances they may not be able to pay any interest. Finally and gradually they may go bankrupt. Hence it is always necessary to mobilize funds of commercial banks in the form of loan and advances.

The ratio of Loan and Advances to Total Deposit reveals the loan and advance situation of commercial banks. It shows how much of their deposit is utilized in the form of loan and advances. While disbursing deposit as loan and advance banks must act prudently. Banks deals with many people known as its clients in the form of depositor, creditor and other stake holders. These clients have their own problem and demands. They approach banks with different demands and problems.

Banks have to disburse money to lenders and borrowers. So bank must have certain money to meet the needs of borrowers and lenders. Banks cannot use all deposits as loan and advance. Meantime bank cannot preserve deposit without using as loan and advances because they are obliged to meet the interest of deposit.

The ratio is calculated by dividing Total Loan and Advances by total deposit as follow:

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

Table 4.1

Total Loan and Advances to Total Deposit Ratio

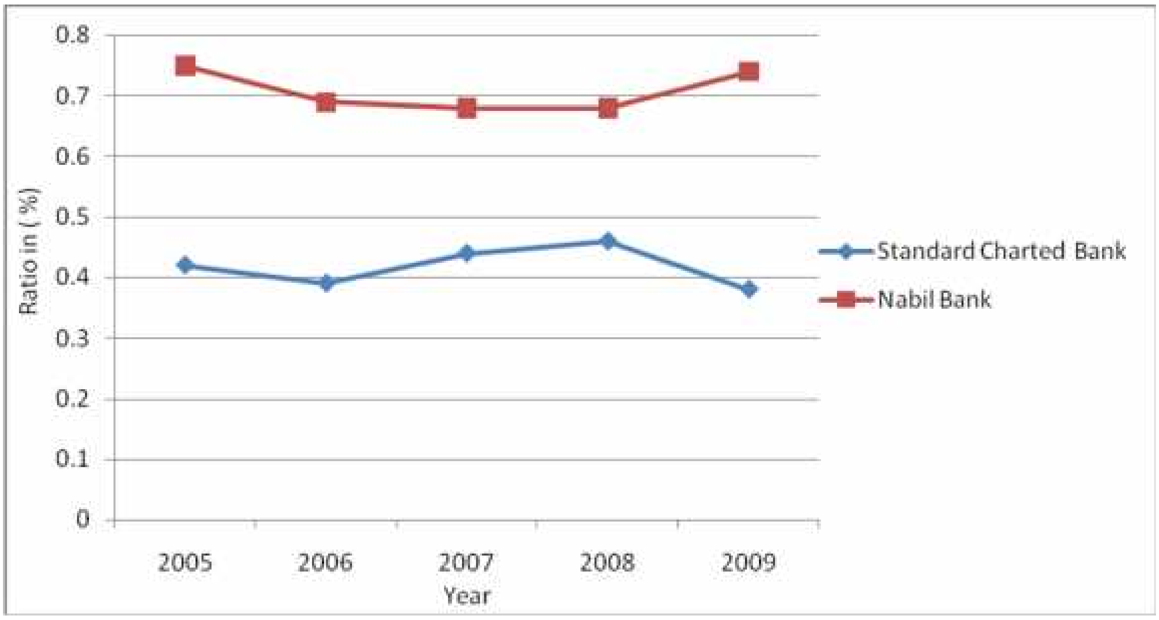
(Rs. In Millions)

Name	**Standard Charted Bank**					**Nabil Bank**				
Year (Mid-July)	Total Loan and Advances	Index %	Total Deposit	Index %	Ratio	Total loan and advances	Index %	Total Deposit	Index %	Ratio
2005	8143	100	19364	100	0.42	10947	100	14587	100	0.75
2006	8935	109.73	23061	119.09	0.39	13279	121.30	19347	132.63	0.69
2007	10790	120.76	24640	120.71	0.44	15903	119.76	23342	120.65	0.68
2008	13719	127.15	29743	120.67	0.46	21365	131.35	31915	136.73	0.68
2009	12680	99.72	35871	120.60	0.38	27590	129.14	37348	117.02	0.74
Mean	11053.4		**26535.8**			17816.8		25307.8		
SD	2325.16		**5736.46**			5979.63		8281.94		
CV(%)	**21.04**		**21.6262**			**33.56**		**32.72**		

Source: Financial Report of Bank

Figure 4.1

Total Loan and Advances to Total Deposit Ratio



The above table reveals the ratio of Total Loan and Advances to the Total Deposit of the bank. The ratio is dispersed between 0.38 and 0.46 for SCBL. The highest ratio is 0.46 and the lowest ratio is 0.38 of SCBL. The ratio is fluctuating.

It means the ratio of Loan and Advances to the total Deposit ratio is fluctuating. Thus ratio is important indicator of the performance of bank because it reveals the competence of the bank to disburse its deposit fund as loan and advance to the various sectors. This is also important for the overall economy of the country. Loan and advance goes to entrepreneurs who will help in economic growth and economic development.

Same way the ratio of NABIL Bank is dispersed between 0.68 to 0.75. The highest ratio is 0.75 and lowest ratio is 0.68. The ratio is gradually increasing from 2001 to 2005. The maximum ratio 0.75 has reached in 2005 but in 2007 it has again declined to 0.68. Average loan and advances of Nabil bank is higher than SCBL but average deposit collection of SCBL is higher than Nabil Bank. So the inverse condition reflects the attitude of management in these two banks. In SCBL even though higher deposit is collected but it has disbursed it in the form of loan and advances cautiously.

4.1.2 Loan Loss Provision to Total Loan and Advance Ratio

Loan loss provision is mandatory because of Nepal Rasta Bank's Central bank, directives. Loan loss provision varies according to the nature of loan. Loan is classified on the basis of time period. If loan is not paid in stipulated time then on the basis of time these loans are categorized into bad loan, loss loan, etc. to recover and to minimize the risk of ordinary depositors from banks mismanagement NRB has obliged commercial banks to form provision.

Loan lending is major function of commercial banks .Commercial banks have to lend deposit in the form of loan and advances. Obviously it is the major source of profit of the commercial banks. But it inherent risk too. This risk is due to bad motive of management of banks and even sometimes lenders approach with wrong intention .So banks have to be cautious in dealing with loan disbursement.

Loan loss provision to total loan and advance ratio express the loan loss provision to total loan and advances. Higher the ratio implies that much of the fund of bank remained unproductive as reserve.

The Ratio is Calculated Using Following Formula

Loan loss provision to Total Loan and Advance Ratio= $\frac{\text{Loan and loss Provision}}{\text{Total loan and advance}}$

Table 4.2

Loan Loss Provision to Total Loan and Advance Ratio

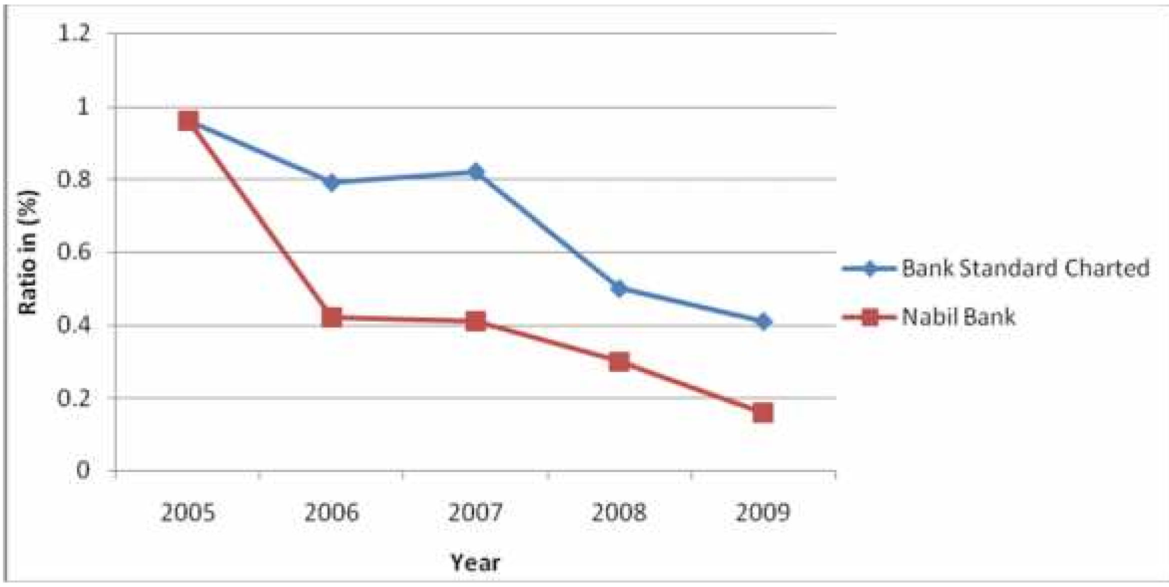
(Rs. In Millions)

Name	**Standard Charted Bank**					**Nabil Bank**				
Year (Mid-July)	Loan Loss Provision	Index	Total loan and Advance	Index	Rat%	Loan loss Provision	Index	Total loan and Advance	Index	Ratio%
2005	78	100	8143	100	0.96	61	100	10947	100	0.96
2006	71	91.03	8935	109.73	0.79	56	91.80	13279	121.30	0.42
2007	88	91.03	10790	120.76	0.82	65	166.07	15903	119.76	0.41
2008	69	78.41	13719	127.15	0.50	64	98.46	21365	134.35	0.30
2009	56	81.16	13680	99.72	0.41	45	70.3	37590	129.14	0.16
Mean	72.4		11053.4			58.2		17816.8		
SD	10.56		2325.16			6.95		5979.63		
CV (%)	14.58		21.04			11.94		33.56		

Source: Financial Reports of Banks

Figure 4.2

Loan Loss Provision to Total Loan and Advance Ratio



Above table shows the ratio of Loan Loss Provision to the Total Loan and Advances. If the provision increases it will retain fund of the bank as non-productive resource. The provision held is for the security of non-performing loan and advances as stipulated by central bank's directive.

In the above table the ratio is gradually declining. In the year 2004 it was 0.96% but it has declined to0.41% in the year 2009 of SCBL. But in years 2007 it has slightly gone up but then year 2006 then it has fallen. It implies bank management of SCBL is conscious and cautious about the affects of the provision in the overall performance of the bank so it has made efforts to decline it gradually.

In case of NABIL Bank also the ratio is tapering continuously. In 2005 it was 0.96% but it has reduced to 0.16% only in the year 2009. So it has reduced significantly in the study period. It also reveals the attitude of management towards the consequences of LLP.

Within the study period average LLP of SCBL is higher than Nabil Bank. Average LLP of SCBL is Rs 284.572.4 million but the average LLP of Nabil Bank is Rs.

58.2 million. Same way consistency level of LLP is higher in SCBL than Nabil bank. The CV of LLP of SCBL is 14.58% where as Nabil Bank has 11.94%. It means management of Nabil is guardedly tapering the LLP so that the effect of LLP can be reduced as far as possible.

LLP and total loan and advance Index of SCBL is declining in 2006 and invested in 2007 and again decreased in 2008 and 2009.

4.1.3 Non- Performing Loans to Total Loan and Advance Ratio

Non- performing assets, also called non-performing loans, are loans on which repayments or interest payments are being made on time.

A loan is an asset for a bank as the interest payments and the repayments of the principal create a stream of cash flows. It is from the interest payments a bank makes its profits.

Banks usually treat assets as non-performing if they not serviced for some time. If payments are late for a short time a loan is classified as past due. Once a payment becomes really late the loan classified as non-performing.

Increase in the amount of non-performing assets or loans means mismanagement of loan and deposit of individuals and households. Profitability of bank may dwindle. So commercial banks need to reduce non-performing assets or loans.

The Ratio of NPL to total loan Advance reveals how much or the loan and advances are non-performing assets.

It is calculated as follow = $\frac{\text{Non-Performing loan}}{\text{Total Loan and Advances}}$

Table 4.3

Non-Performing Loan to Total Loan and Advance

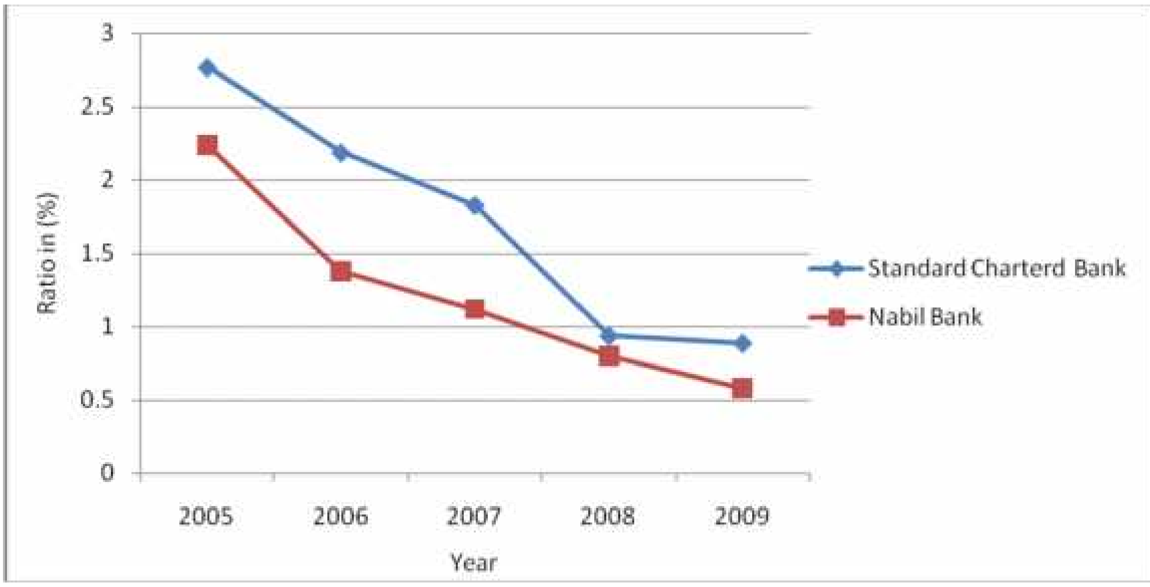
(Rs. In Millions)

Name	Standard Chartered Bank					Nabil Bank				
Year (Mid-July)	Nonperforming loan	Index	Total Loan and advances	Index	Ratios (%)	Nonperforming loan	Index	Total Loan and advances	Index	Ratios (%)
2005	226	100	8143	100	2.77	245	100	10947	100	2.24
2006	196	88.73	8935	109.73	2.19	183	74.69	13279	121.3	1.38
2007	197	100.5	10790	120.76	1.83	178	97.27	15903	119.76	1.12
2008	129	65.48	13719	127.58	0.94	171	96.06	21365	134.35	0.80
2009	123	95.35	13680	99.72	0.89	159	92.98	27590	129.14	0.58
Mean	174.2		11053.4			187.2		17816.8		
SD	48.85		2325.16			30.47		5979.63		
CV(%)	23.45		21.04			16.27		33.56		

Source: Financial Reports of Banks

Figure 4.3

Non-Performing Loan to Total Loan and Advance Ratio



Above table shows the ratio of Non- performing loan to the total Loan and Advances. Average non-performing loan of the bank within the study period Rs 174.2 million and SD is Rs 48.85 million and CV is 23.45% of SCBL. Same way average loan and advances bank has disbursed within study period Rs 11053.4 million and SD is Rs 2325.16 and CV is 21.04% of SCBL.

The ratio is sharply falling. In the year 2005 the ratio was 2.77 and in the year 2009 it was 0.89%. Every year within the study period it is just decreasing. It means bank management is conscious and cautious about the affects of NPL so it trying to reduce it every year in big chunk.

In other hand Nabil Banks average NPL is Rs 187.2 million and SD is Rs 30.47 million and CV is 16.27%. Banks average loan and advance disbursement is Rs 17816.8 million and SD of Loan and Advances is Rs.5979.63 million and CV is 33.56%.

The ratio of NPL to Total Loan and advances is sharply declining. In the year 2005 NPL was Rs 245 million but it has reduced by about 1/5 times in the year

2009to RS 159 million. The ratio also declined sharply from 2.24 to 0.58. This indicated the management's attitude towards NPL. Bank is trying to reduce the NPL amount.

4.1.4 Non-Performing Loan to Total Deposit

Commercial banks' major function is to collect deposit and disburse it in the form of loan and advances. When loan and advances are lent there is risk. Some lenders may be able to pay because of bankrupt or some may turn cheat. According to the directive to NRB commercial banks has to categorize loan and advances based upon the repayment time into productive or non productive loan. Productive loan help to enhance performance of bank and also help in boosting economic situation of country. But non-productive loan known as non-performing loan erodes not only the performance of the bank but also economy of country. So collected deposit must be used wisely. The ratio of NPL to Total Deposit indicated the relationship between NPL and Total Deposit. It is calculated:

$$\text{Non-Perfuming Loan to Total Deposit} = \frac{\text{Non-performing}}{\text{Total Deposit}}$$

Table 4.4

Non-performing Loan to Total Deposit

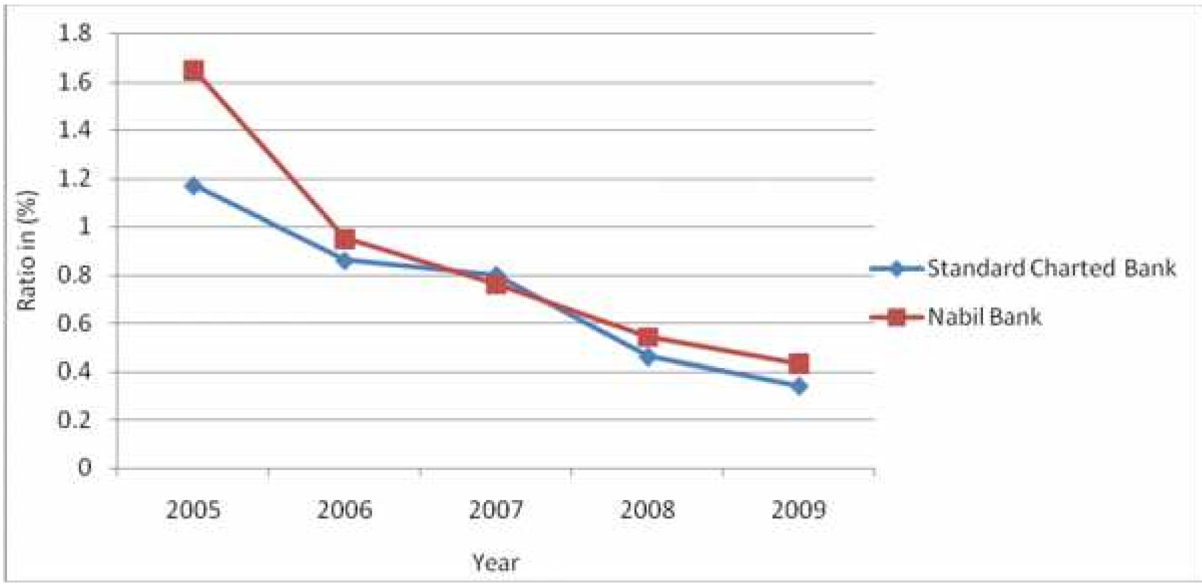
(Rs. in Millions)

Name	**Standard Charted Bank**					**Nabil Bank**				
Year (mid-July) 2009	Non-performing Loan	Index	Total Deposit	Index	Ratio (%)	Non-Performing Loan	Index	Total Deposit	Index	Ratio (%)
2005	226	100	19364	100	1.17	245	100	14587	100	1.65
2006	196	86.72	23061	119.09	0.86	183	74.69	19347	132.63	0.95
2007	197	100.51	24640	106.85	0.8	178	97.27	23342	120.65	0.76
2008	129	65.48	29743	120.71	0.46	171	96.06	31915	136.73	0.54
2009	123	95.34	35871	120.60	0.34	159	92.98	37348	117.02	0.43
Mean	174.2		26535.8			187.2		25307.8		
SD	48.85		5736.46			30.47		8281.94		
CV (%)	23.45		21.62			16.27		32.72		

Source: Financial Reports of Banks

Figure 4.4

Non-performing Loan to Total Deposit Ratio



In the table ratio of the NPL to Total Deposit of SCBL is gradually declining. In year 2005, 2006, 2007, 2008 and 2009 the ratio is 1.17, 0.86 0.80 0.43 and 0.34 respectively. In case of Nabil bank also the ratio is gradually declining. In year 2005 it was 1.65 and it is gradually declining. In the Both banks are reducing the proportion of NPL to total deposit.

In the table Index of the NPL to Total Deposit of SCBL is gradually declining. In 2006, 2007, 2008 and 2009. And index is 89.68, 86.72, 100.5, 65.48 and 95.34 total deposit is declining. In case of Nabil Bank also index is NPL is declining gradually.

4.1.5. Loan Loss Provision to Non-Performing Loan

Loan loss provision is reserve created to save individual and households savings. Commercial banks have to maintain certain percentage as loan loss provision on the basis of the nature of loan. Higher the NPA higher the Loan loss Provision. If Loan loss provision is higher, it may curtail the performance of bank. If NPA is higher, it has to create higher loan loss provision. Higher loan loss provision is trained from its available funds which otherwise can be used as productive fund.

The ratio of loan loss provision to NPA shows the relationship between them. What is its trend? Is it increasing or decreasing? The ratio is calculated using following formula:

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

Table 4.5

Loan Loss Provision to Non-Performing Loan

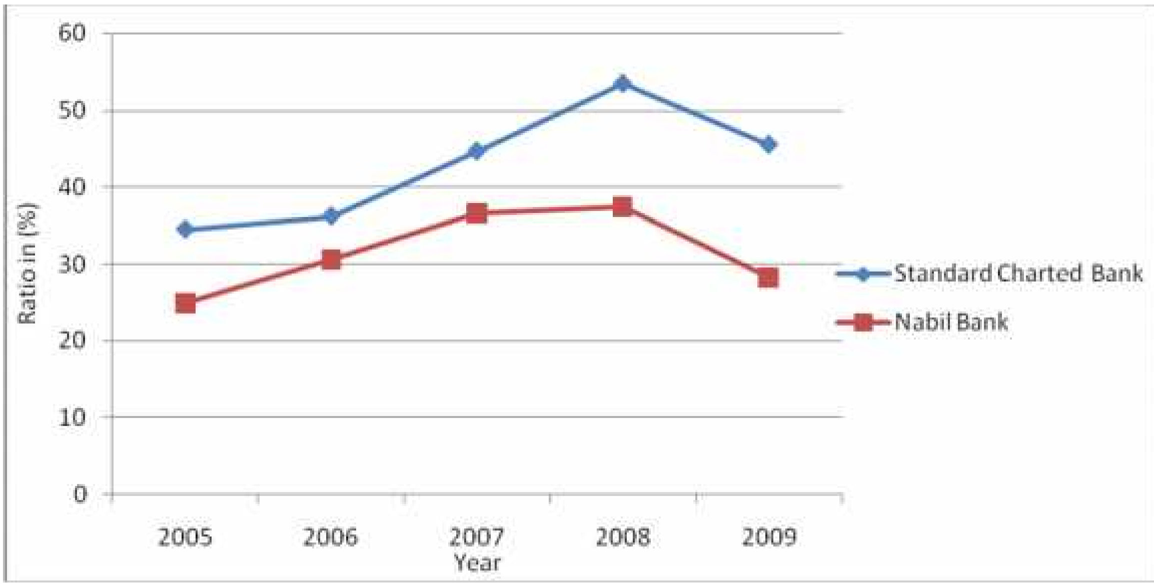
(Rs. in Millions)

Name	**Standard Charted Bank**					**Nabil Bank**				
Year (mid-July)	Loan Loss Provision	Index	Non-performing Loan	Index	Ratio (%)	Loan Loss Provision	Index	Non-Performing Loan	Index	Ratio (%)
2005	78	100	226	100	34.5	61	100	245	100	24.90
2006	71	91.03	196	86.72	36.22	56	91.80	183	74.69	30.60
2007	88	123.94	197	100.52	44.67	65	86.45	178	97.27	36.52
2008	69	78.4	129	65.48	53.49	64	98.46	171	96.06	37.43
2009	56	81.16	123	95.34	45.53	45	70.31	159	92.98	28.30
Mean	72.4		174.2			58.2		187.2		
SD	10.56		48.85			6.95		30.47		
CV	14.58		23.45			11.94		16.27		

Source: Financial Reports of Banks

Figure 4.5

Loan Loss Provision to Non-Performing Loan



The table shows the ratio of loan loss provision to non-performing loan. The ratio is in fluctuation that means the ratio is increasing some time and decreasing next time. In the years 2005, 2006, 2007, 2008 and 2009 the ratio is 0.34, 0.36, 0.45, 0.53, and 0.46 respectively of SCBL. The average loan loss provision in the study period is Rs 72.4 million. The standard deviation of the loan loss provision is Rs 10.56 million. There is less variation in loan loss provision because CV is only 14.58%. Average Non- performing loan within the study period is Rs. 174.2 million. Its SD is Rs 48.85 million and CV is 23.87%.

The ratio of loan loss provision to the Non-performing loan is fluctuating. Loan loss provision to the Non-performing loan is directly related. As the NPL increases LLP also increases. Although the ratio is fluctuating, it remained somewhat near 0.4. That means bank is trying to maintain the ratio constant at minimum.

In case of Nabil bank the ratio is fluctuating. The ratio is highest in year 2005 that is 24.90% which is lowest in year 2005 and 2008that is 37.43%. But in year 2009 it has reduces to 228.30%.

The Index of Loan loss provision to the Non-performing loan is fluctuating in both in Standard chartered bank and Nabil bank. The Index is highest in the 2007 in Nabil bank i.e. 100.5 and in case of Standard chartered bank the index is highest in the year 2007 i.e. 123.94.

4.1.6. Net Profit to Total Loan and Advances

Net Profit reveals the performance of bank. It shows efficiency of management. It shows the capacity of management has been able to utilize deposits. Net profit increment plays vital role of the bank.

The ratio of net profit to total loan and advances reveals profit in comparison to total loan and advance disbursed.

It is calculated using following formula = $\frac{\text{Net-Profit}}{\text{Total loan and Advances}}$

Table 4.6

The Ratio of Net-Profit to Total Loan and Advance

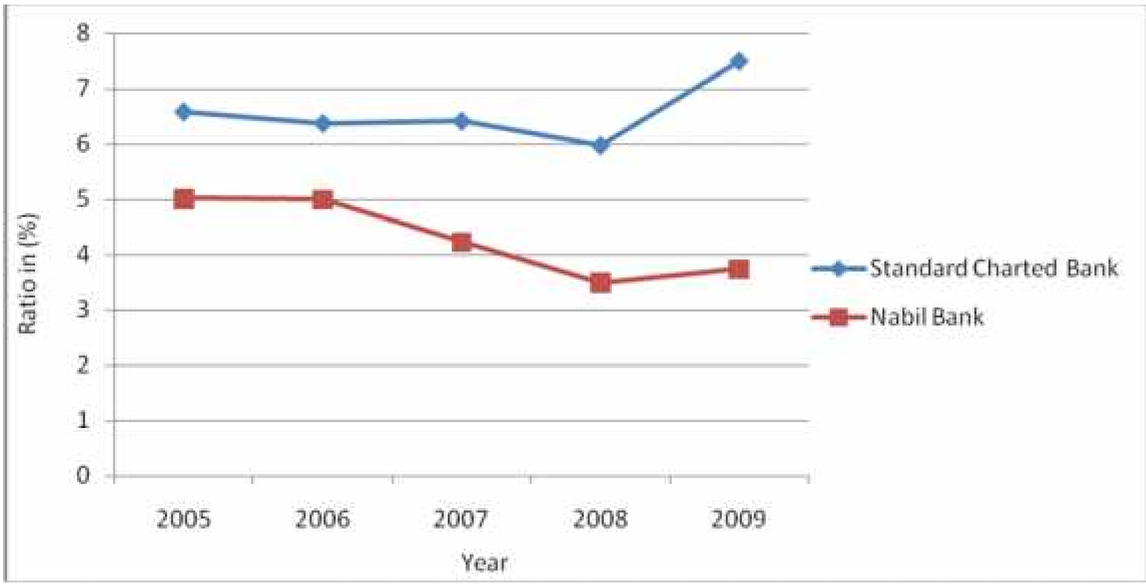
(Rs in Millions)

Name	**Standard Charted Bank**					**Nabil Bank**				
Year (mid-July)	Net Profit	Index	Total Loan and Advances	Index	Ratio (%)	Net Profit	Index	Total Loan and Advances	Index	Ratio (%)
2005	536	100	8143	100	6.58	550	100	10947	100	5.02
2006	659	122.95	8935	109.73	6.37	665	120.91	13279	121.30	5.00
2007	692	105.01	10790	120.76	6.41	673	101.2	15903	119.76	4.23
2008	819	118.35	13719	127.15	5.97	746	110.85	21365	134.35	3.49
2009	1025	125.15	13680	99.72	7.49	1031	138.2	27590	129.14	3.74
Mean	746.2		11053.4			733		17816.8		
SD	165.98		2325.16			161.67		5979.63		
CV (%)	22.24		21.04			22.06		53.56		

Source: Financial Reports of Banks

Figure 4.6

The Ratio of Net-Profit to Total Loan and Advance



The given table reveals the ratio of Net profit to Total Loan and Advances and Indexes. The ratio of SCBL is 6.58, 6.37, 6.41,5.97, and 7.49 in the years 2005, 2006, 2007, 2008 and 2009 respectively. The average Net profit within the study period is Rs 746.2 million and its SD is Rs 165.98 million and CV is 22.24%. Same way average loan and advances within the study period is Rs 11053.4 million and SD is 2325.16 and CV 21.04%. Net profit is gradually increasing during the period in comparison to the loan and advances.

In case of NABIL Bank the ratio is 5.02, 5.00, 4.23, 4.49 and 3.74 in the years 2005, 2005, 2006, 2007, 2008 and 2009 respectively. The average net profit within the study period is Rs 733 million and SD is 161.67 million and CV is 22.06% same way average loan and advances within the study period is Rs. 17316.8 million, SD is Rs.5979.63 million and CV is 33.56%. The ratio is gradually decreasing in 2008 during the study period. It means bank is unable to harp more profit from its loan and advances

From the above table the Index of Net profit in the Standard Chartered bank is gradually increasing from year 2005 to 2008 and slightly decreased in year 2009.

Same way loan and advance is slightly decreased in the year 2009 and it gradually increasing from year 2005 to till 2008.

In the case of Nabil bank the Index is fluctuating i.e. 120.91, 101.2, 110.85 and 138.2 in the year 2006, 2007, 2008 and 2009 respectively. And same as in total loan and advance.

4.2 Correlation

Correlation defines two or more variables are correlated with each other or not. The correlation between variables varies from -1 to 0 to +1. If two variables are inversely correlated then they have negative correlation, whereas if they are highly correlated or proportionately correlated then they have positive value. If value is between 0.7 and 1, then they are highly correlated.

For the purpose of decision-making interpretation of the result is based upon following conditions:

When r = 1, there is perfect positive correlation

When r = 1, there is perfect negative correlation

When r = 0, there is no correlation

When r lies from 0.7 to 0.999 (-0.7 to -0.999), there is a high degree of positive (or negative) correlation.

When r lies from 0.5 to 0.6999, there is moderate degree of correlation.

When r is less than 0.5, there is low degree of correlation.

4.2.1 Correlation Between Loan Loss Provision and Loan and Advances

The co-efficient shows the degree of relationship between Loan loss Provision and Loan and Advances. Here, Total loan and advance is considered as independent variable (x) and loan loss provision is dependent variable (y). The below table describes the total relationship between Loan Loss provision and Loan and Advances, during the study period.

Table 4.7(a)

Correlation Co-efficient Between Loan Loss Provision and Loan and Advances for Standard Charted Bank

r	P.E.(r)	6P.E.(r)
-0.52	0.22	1.32

Source : Annex 1

Table 4.7(b)

Correlation Co-efficient Between Loan Loss Provision and Loan and Advances for Nabil bank

r	P.E.(r)	6P.E.(r)
-0.063	-0.2004	1.802

Source: Annex 2

The table 4.7 (a) reveals that the coefficient of correlation between Loan loss Provision and Loan and Advance of Standard Chartered Bank Limited, the value is negative 0.52(-0.52). It means there is negative moderate degree of correlation between Loan loss Provision and Total Loan and Advances.

The value of P.E. (r) is 0.22 and the value of 6P.E. (r) is 1.32. So value of r is less than 6 P.E. so the value of correlation is insignificant. It implies there is no significant relationship between loan loss provision and the total loan and advances disbursed. On the other hand table 4.7(b) reveals the coefficient of correlation between LLP and Loan and advances of Nabil bank is negative 0.063 (-0.063). It means there is very low negative correlation between LLP and Loan and Advances in case of Nabil bank. The value of P.E. (r) is 0.3004 and 6P.E. (r) is 1.802. Value of r is less than the value of 6P.E. (r). It means there is insignificant relation between LLP and Loan and Advance.

4.2.2 Correlation between Loan Loss Provision and Non-Performing Loan

To measure and evaluate the co-efficient of correlation between these two variables i.e. loan loss provision (LLP) and non-performing loan (NPL). In this analysis, LLP (y) is taken as dependent variable and NPL is taken as independent justify whether LLP and NPL are highly significant or not. The following table describes the relationship between LLP and NPL within study period.

Table 4.8(a)

Correlation co-efficient between LLP and NPL of SCBL

r	P.E	6P.E
0.746	0.134	0.803

Source: Annex 3

Table 4.8(b)

Correlation co-efficient between LLP and NPL of Nabil Bank

r	P.E.(r)	6P.E.(r)
0.353	0.264	1.584

Source: Annex 4

From the table 4.8(a) it is revealed that the correlation co-efficient between LLP and NPL of the SCBL is positive correlation between two variables. In another word, as NPL increase LLP also increases but at very low rate. The value of P.E. is 0.134 and 6P.E is 0.803. The value of r is less than 6 P.E. that means there is significant relation between LLP and NPL. It implies that increment in LLP is not the result of increment of NPL.

In table 4.8(b) the correlation coefficient between LLP and NPL of Nabil bank is positive 0.353 (+0.353), it means that there is high degree of positive correlation between these two variables. In another word, as NPL increases LLP also increases significantly. The value of P.E. (r) is 0.264 and the value of 6P.E. (r) is

1.584. The value of r is less than the value of 6P.E. (r). It implies that the relationship between NPL and LLP in Nabil bank is insignificant.

4.2.3 Correlation between Total Loan and Total Advances and Deposit

The calculation was conducted to find out the relationship between loan and advances and total deposit. The table given below shows the correlation between loan and advances and deposit within the study period.

Table 4.9 (a)

Correlation between Loan and Advances and total Deposit of SCBN

r	P.E	6P.E
0.927	0.0424	0.255

Source: Annex 5

Table 4.9 (b)

Correlation between Loan and Advances and total Deposit of Nabil Bank

r	P.E.(r)	6P.E.(r)
0.989	0.007	0.04

Source: Annex 6

The table 4.9(a) shows the value of r is positive 0.927(+0.927) which is highly positive in case of SCBL. And again P.E is equal to 0.0424 and 6P.E. is 0.255. The positive value of r means that when deposit increases loan and advances also increases. So one has influence upon another in the positive form.

The value of 6P.E. is less than r, i.e. the value of coefficient of correlation is higher than 6P.E. this implies that there is significant relationship between deposit collected and loan and advances disbursed.

The table 4.9(b) shows the value of r is positive 0.989 (+0.989) which is highly positive in case of Nabil Bank. The value of P.E. (r) is 0.007 and 6P.E. (r) is 0.04. The value of r indicates that there is highly positive correlation between Loan and

Advances and Total Deposit. If total Deposit increases Loan and advances also increases. The value of 6P.E. (r) is less than the value of r. It means there is significant relationship between two variables.

4.3 Trend Analysis

Trend analysis is done to predict the future scenario. This analysis is very important for business. Business environment is more complex and dynamic than ever before so firms want to know will- be scenario. This scenario helps to build strategies and tune to the unseen changes in the economy. So this statistical tool helps businessmen to estimate future. The estimation is based upon past data or information

Among various methods of estimating trend the least square method is used in this research. In this method trend line is fitted to the data satisfying following two conditions:

$$\sum y = na + b\sum x$$

$$\sum xy = a\sum x + b\sum x^2$$

4.3.1 Trend analysis of Loan and Advances

In the calculation time is taken as independent variable (x) and loan and advance is taken as dependent variables(y). The calculation is made to estimate trend of loan and advance from 2001 to 2014. The trend of loan and advances is forecasted from the year 2009 to 2014 based upon the past data.

Table 4.10(a)

Trend of Loan and Advances for SCBL

(Rs. in Millions)

Year	2010	2011	2012	2013	2014
Estimated Loan and Advances	15810.8	17896.6	18982.4	20568.2	22154

Source: Annex 14

Table 4.10(b)

Trend of Loan and Advances for Nabil Bank

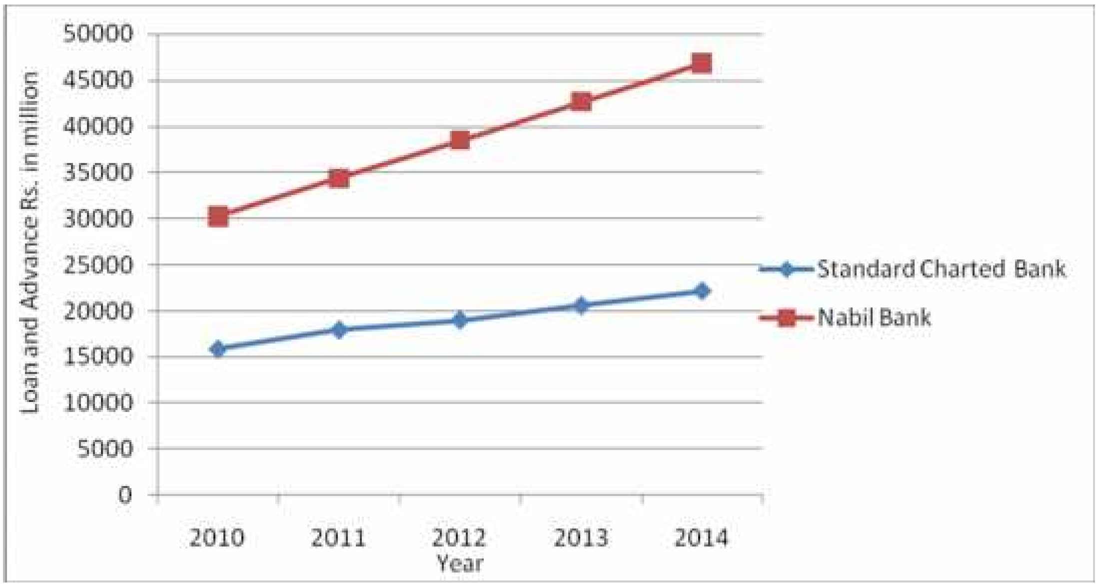
(Rs. In Millions)

Year	2010	2011	2012	2013	2014
Estimated Loan and Advances	30228.4	34365.6	38502.8	42640	46777.2

Source: Annex 15

Figure 4.7

Trend of Loan and Advances



As shown in the table 4.10(a) loan and advance is in increasing trend. If the business environment remains same the SCBL will be able to disburse Rs 22154 Million in year 2014. This is the highest amount of loan and advance it will be able to disburse.

In table 4.10(b) it shows the loan and advance in future years of Nabil Bank. It also shows that loan and advances is increasing. The maximum loan and advances will be in year 2014, which will amount to Rs46777.2 million.

4.3.2 Trend Analysis of Loan Loss Provision

Loan loss provision is unproductive fund from the view of bank management. Bank has to allocate fund in the form of loan loss provision. As the directive of central bank, Nepal Rastra Bank is mandatory for any commercial banks operating in the land they have to allocate fund as loan loss provision. Loan loss provision is allocated on the basis of nature of loan. Nature of loan categorized on the basis of time of repayment. Trend of loan loss provision is calculated below:

Table 4.11(a)

Trend of Loan Loss Provision for SCBL

(Rs. in Millions)

Year	2010	2011	2012	2013	2014
Estimated Loan Loss Provision	58.6	54	49.4	44.8	40.2

Source: Annex 7

Table 4.11(b)

Trend of Loan Loss Provision for Nabil Bank

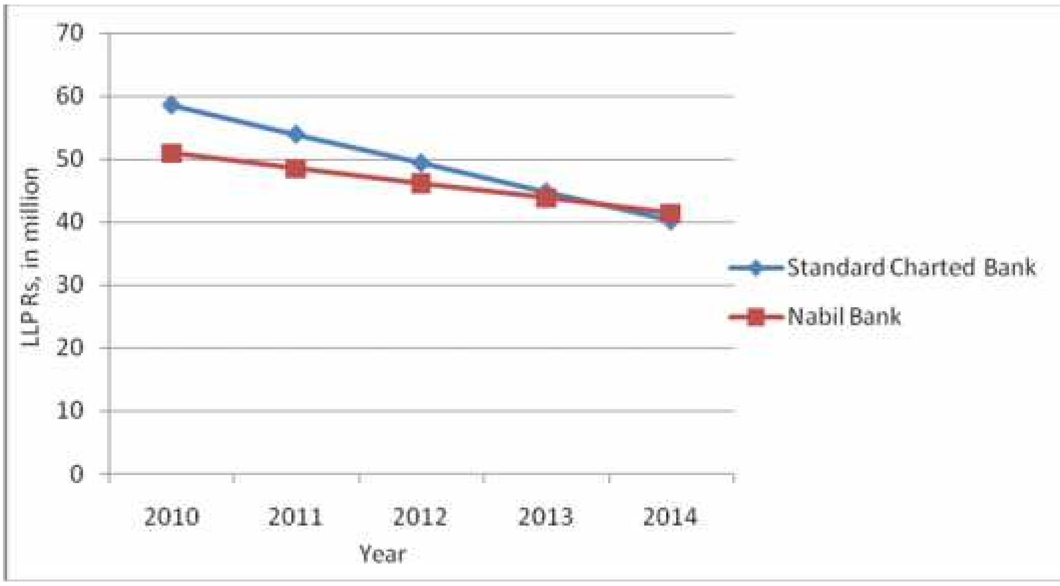
(Rs .in Millions)

Year	2010	2011	2012	2013	2014
Estimated Loan Loss Provision	51	48.6	46.2	43.8	41.4

Source: Annex 8

Figure 4.8

Trend of Loan Loss Provision



Above table 4.11(a) reveals the trend of Loan loss provision from year 2010 to 2014 of SCBL. The trend is decreasing. In the year 2010 it is Rs 58.6 million but in 2014 it will be Rs 40.2 million. The trend is calculated based upon the past information. From year 2010 to 2014 the trend of Loan loss provision is estimated based on the historical data. So within the estimated period if the business environment remains same trend of Loan loss provision will gradually decline. Gradual declination of LLP means it can use the unproductive fund in some productive fund and increase its net profit

Also in table 4.11(b) trend of LLP in Nabil Bank is revealed. The bank will have 51 Millions as LLP in 2010 but it will be reduced to Rs.41.4 Million in 2014. This is based upon the historical data and assumption of status quo.

4.3.3 Trend Analysis of Non-performing Loan

NPL reduces and hinders the performance of bank. It also reduces the credibility of bank. So banks have to reduce NPL to increase productivity and profitability. Trend of NPL of banks is estimated below:

Table 4.12 (a)

Trend of Non- Performing Loan of SCBL

(Rs in Millions)

Year	2010	2011	2012	2013	2014
Estimated NPL	92.3	65	37.7	10.4	-16.9

Source: Annex 9

Table 4.12 (b)

Trend of Non-Performing Loan of Nabil Bank

(Rs in Millions)

Year	2010	2011	2012	2013	2014
Estimated NPL	132	113.6	95.2	76.8	58.4

Source: Annex 10

Figure 4.9

Trend of Non- Performing Loan

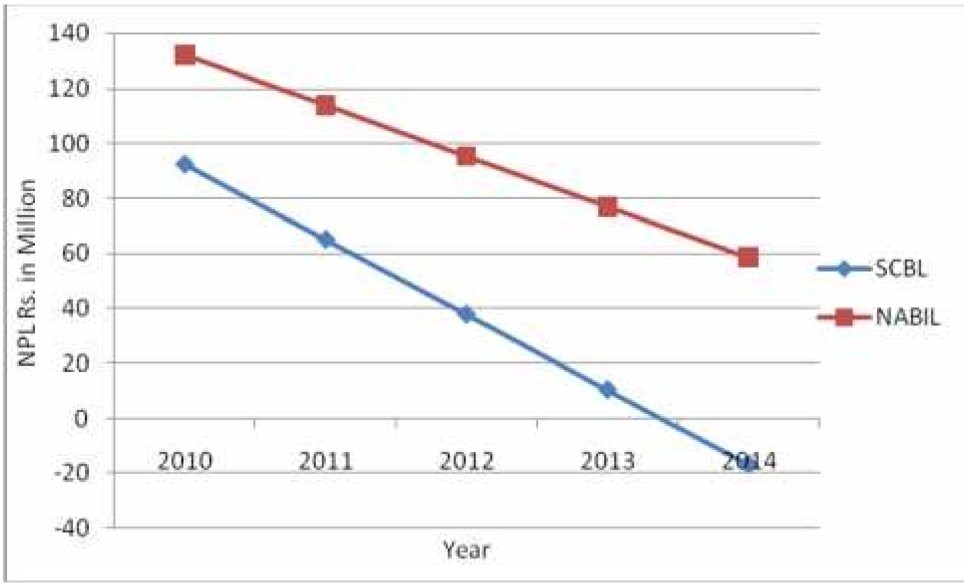


Table 4.12(a) shows that the Trend of Non-performing loan is gradually declining. It has reached to Rs -16.9 million in 2014 from the year 2010 when it is Rs 92.3 Million. The negative amount means virtually there will not be any NPL of the SCBL in year 2014. So it is decreasing sharply. This trend is good for the bank. Bank is able to utilize resources in productive sources. So bank will continuously

decrease its Non- performing loan in coming days if the economic environment remains same as the past performances were occurred.

In the table 4.12(b) also shows the trend of NPL is gradually declining. In the year 2010 it is Rs. 132 million and in the year 2014 it will be Rs58.4 million. So bank will continuously decrease its non-performing loan in the coming year if the economic condition remains same as the past performances occurred.

Trend Analysis of Net-Profit

Net profit is the major objectives of any business. It attracts to invest more in the industry. It encourages entrepreneur to introduce new technology, new product. It also shows the competence of management to operate in the given business environment. It also shows the health of the firm or company. Trend analysis is conducted to predict future net profit. The trend is as follows:

Table 4.13 (a)

Trend Analysis of Net- Profit of SCBL

(Rs in Millions)

Year	2010	2011	2012	2013	2014
Estimated NP	1087.6	1201.4	1315.2	1429	1542.8

Source: Annex 11

Table 4.13 (b)

Trend Analysis of Net- Profit of Nabil Bank

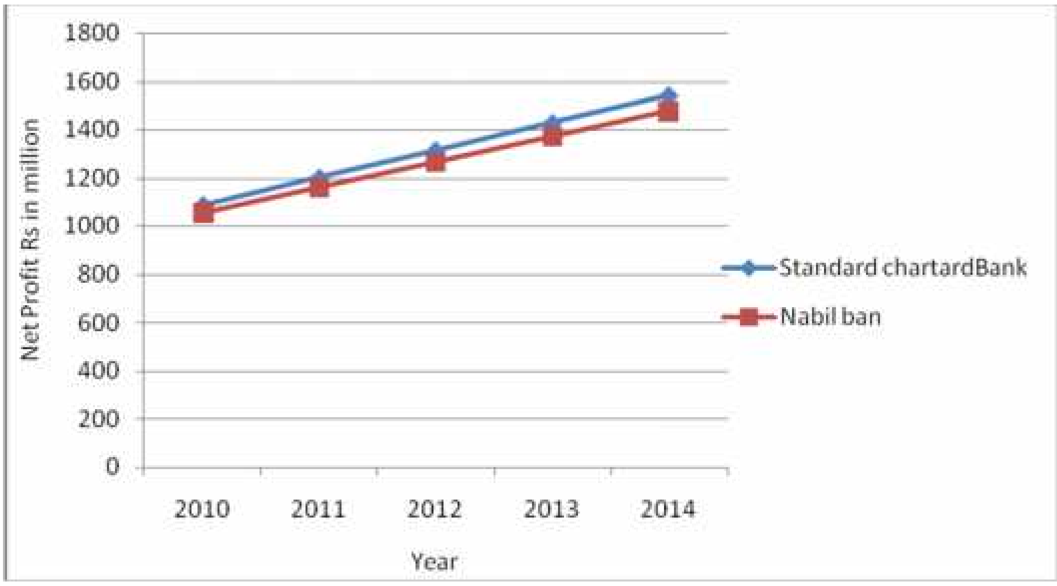
(Rs in Millions)

Year	2010	2011	2012	2013	2014
Estimated NPL	1054.9	1161	1267.1	1373.2	1479.3

Source: Annex 12

Figure 4.10

Trend Analysis of Net- Profit



In the above table 4.10 (a) trend of net-profit is increasing. It is Rs 1087.6 million in year 2010 and it will increase to Rs 1542.8 million in the 2014, if the business environment remains constant. From the year 2010 to 2014 the prediction has been made based upon the historical data from the year 2005 to 2009.

In the table 14.3 (b) trend of Net profit is increasing if the business environment remain status quo. In the year 2010 estimated net profit is Rs. 1054.9 million and in 2014 it will increase to Rs. 1479.3.

4.4 Major Findings of the Study

Ratios

- The ratio of Total Loan and Advances to Total Deposit of Nabil Bank Ltd. is higher than the ratio of SCBL. The ratio of Nabil Bank is dispersed between 0.67 and 0.75 so the range of dispersed is 0.08 but in case of SCBL it is dispersed between 0.38 and 0.46 and the range is 0.17. It implies Nabil bank is willing to lend loan and advances than SCBL of the deposit it has collected. Within the study period Nabil bank has been able to disburse more average loan and advances than the SCBL despite of Low average Deposit collection. This also shows the attitude towards risk. Comparatively, if loan and advance truly express the attitude towards risk, SCBL bank is risk averse and Nabil Bank is risk seeker. Since CV coefficient of loan and advances of both banks are nearly equivalent there is consistency in disbursement of loan of banks. In case of deposit collection SCBL has been able to collect more amount than the Nabil bank. The coefficient of CV of total deposit of SCBL is higher than the NABIL bank.

- Both banks are trying hard to decrease the ratio to the lowest level as far as possible. In the years 2005, 2006, 2007, 2008 and 2009 both banks have loan loss provision ratio less than 1% respectively. It reveals the consequences of Loan Loss Provision in the bank's performance. Within the study period average LLP of the NABIL bank is less than the SCBL bank. Same way CV coefficient reveals that there are fewer consistencies in the LLP of SCBL bank than Nabil bank.
- The ratio NPL to Total Loan and Advances of both banks is defining but the rate of declining in same ratio in and Nabil bank and SCBL. Within the study period, initially in 2005 the ratio of Nabil bank is higher than the SCBL bank. The ratio is 2.24 of Nabil bank but it 2.77 of SCBL in 2005. But in final year 2009 the ratio of Nabil bank is less than that of SCBL. In 2009 the ratio is 0.58% of Nabil bank and 0.89% of SCBL bank. This clearly indicated that the management of NABIL bank has been able to reduce NPL sharply than SCBL even though the average loan and advances of Nabil bank is higher than SCBL. Average NPL of Nabil bank is higher than the SCBL it may be due to the higher Loan and advances.
- This NPL to Total Deposit ratio is also gradually reducing. The ratio of SCBL is lower than the ratio of Nabil. Average deposit collection of SCBL is higher than of Nabil but the average NPL of SCBL is lower than Nabil. The rate of declining in the ratio is higher in SCBL than Nabil. In 2005 the ratio of SCBL is 1.77 whereas that of Nabil is 1.65. In 2009 the ratio of SCBL is 0.38 and Nabil is 0.43 the lowest value of both banks. Even between the

lowest values Nabil has higher one. It indicated that the collected deposit is gradually turning to productive loan. In another word Loan and advances disbursed from the collection of ordinary people as total deposit is having a fruitful consequence in the economy.

- The LPP to Total NPL ratio of both banks is fluctuating. That means it is increasing some year and decreasing next year. In 2005 the first year within study period, the ratio of SCBL is 0.35 but Nabil bank's is 0.25 only. In 2008 the ratio of Nabil bank has increased to 0.37 in the same year SCBL has only 10.53. In case of SCBL the ratio is increasing from 2005 to 2008 for Nabil within same period it is constant in first two consecutive periods and again increased. The greater fluctuation is seen in Nabil than SCBL. The range of SCBL is between 0.35 and 0.53 but the range for Nabil is 0.25 to 0.37.
- The major portion of net profit of commercial banks is contributed by interest earned from the disbursed loan and advances. It means that the net profit indicates the performance of loan and advance. The ratio of Net Profit to Total Loan and advances of the SCBL is higher than the Nabil bank. The ratio of both banks is fluctuating. Although the disbursement of average loan and advance of Nabil bank is higher than the SCBL average net profit of SCBL is higher than the Nabil bank's. The average net profit of SCBL is Rs746.2 million and the average net profit of Nabil bank is Rs. 733 million. The ratio of SCBL range between 5.97 and 7.49 but in case of Nabil it range between 3.49 and 5.02. The highest ratio of Nabil is still lower than the lower ratio of SCBL. It means Nabil has been unable to maintain net profit with the increment of total loan and advances.

Correlation

- The value of correlation between LLP and Total Loan and Advances, r of SCBL is negative 0.52 (-0.52) and the Nabil is negative 0.063 (-0.063). That means there is negative correlation between LLP and Total Loan and advances. In another word, if Loan and advances increases LLP decrease and vice versa. But the value of r of SCBL is more negative than Nabil. It means in SCBL loan and advance and LLP has more negative correlation than Nabil. Since both banks have r less than 6P.E. (r) there is significant relation between LLP and loan and advances.

- The value of correlation between LLP and NPL, r in both banks is positive. It means there is positive relation between LLP and NPL. As NPL rises LLP also rises. But the value of SCBL is higher than Nabil. The value of r of SCBL is 0.746 and Nabil is 0.353. The higher value of SCBL means there is higher degree of positive correlation between LLP and NPL. That means if NPL increases LLP also increase in SCBL. But in Nabil increment of NPL and LLP is less positively correlated. Same way value of 6P.E. (r) of Nabil is higher than the value of r. That means there is no significant relation between LLP and NPL in Nabil bank. Similarly the value of 6P.E.(r) is greater than the value of r in case of SCBL it means there is no significant relation between LLP and NPL.
- The correlation between Loan and Advances and Total Deposit, r of both banks are positive and their values are higher than 0.75. It means there is higher degree of correlation between total Deposit and Total loan and advances. In another word higher the deposit higher will be loan and advances. In both cases the value of 6P.E. (r) is less than the value of r; it also signifies that there is significant relation between Total Loan and Advances. The value of r of SCBL is higher than Nabil.

Trend Analysis

- Trend analysis of Loan and advances of both banks shows the increasing trend of loan and advances. But the ratio of increment of Nabil is higher than the SCBL. In 2014 SCBL will have Rs.22154 million and Nabil will have Rs 46777.7 million as loan and advance. So Nabil bank has to act prudently to cope with various problems due to loan and advances.
- The trend analysis of LLP of both banks is gradually declining. The rate of declining is higher in case of SCBL than Nabil. In the end of estimated

period 2014, the LLP of SCBL will be Rs. 40.2 million only whereas the Nabil will have Rs. 41.4 million. The trend indicated positive aspect of bank.

- The trend analysis of NPL of both banks is also declining. In this case also SCBL's rate of reduction is higher than Nabil. According to trend from 2010 onwards SCBL will not have any NPL in 2014 because of negative amount. But Nabil will have positive amount even 2014 which amounted to Rs 41.4 million.
- Trend of Net profit is increasing in both banks. The rate of increment of SCBL is higher than the Nabil. In 2010 the net profit of SCBL is Rs.1087.6 million and that of Nabil is Rs. 1054.6 million. In year 2014 the net profit of SCBL is Rs. 1542.8 million and Rs. 1479.3 million of Nabil. Profit of SCBL bank will overcome the profit of Nabil Bank in future if the economic environment remains same.

CHAPTER –V

SUMMARY, CONCLUSION AND RECOMMENDATION

This research attempts to analyze the NPL and Loan Loss Provision and their effects in the performance of bank. This chapter is final chapter. It includes summary, conclusion and recommendation. Summary and conclusion of the study is presented in the first section. The second section has been design for the recommendation.

5.1 Summary

Financial sector of have major role to play in the development of the country. Banks are the financial regulator, which collects funds and invest them in productive sectors. There is not so long history of commercial bank in Nepal. Nepal Bank Limited is the first commercial bank established on 1994 Kartik 30. But now there are 26 commercial bank as per NRB *banking and financial statistics* published in mid July 2009 extending their series in different part of the country.

The successful working of the bank depends on ability of the management to distribute the funds among the various kind of investment known as loans and advances. Loan and advances are the most profitable assets of a bank. These assets constitute primary sources of income to the bank. As being a business institution, a bank aims at making huge profit. Since loans and advances are more profitable than any other assets of the banks, it is willing to lend as much as its funds as possible but banks have to be careful about the repayment of loan interest before giving loan.

This study is aimed at studying the non-performing loan and loan loss provisioning of commercial banks. For this purpose, descriptive cum analytical research design was adopted. Out of the total population the twenty six commercial banks, only two banks, SCBL and Nabil banks are taken as joint venture bank as sample using judgmental sampling method. Secondary data are collected from annual reports and other publication of respective banks. The data collected from various sources are recorded systematically and presented in appropriate mathematical, statistical, financial, graphical tools have been applied to analyze the data. The data of five consecutive years of the two selected banks have been analyzed to analyze to meet the objective of the study.

Nepal Rastra Bank has set up the directives/ regulations regarding the loan loss provisioning of the Nepalese commercial banks. According to the this provision a bank has to maintain 1%, 25%, 50% and 100% loan loss provision for its pass , substandard, doubtful and bad loan respectively. It is found that sampled banks maintained higher than requirement for one type of loan where are lower for another class of loan category. They should make provision perfectly neither more nor less. The reason may be over provision create inadequacy of capital which reduce the profit and less provision create legal hassle to the bank. The loan loss provision made by Nabil bank and SCBL found satisfactory not serious matter only little attention is needed to manage LLP of each loan category. Likewise role of NRB is essential, regular supervision and control over the Nepalese commercial banks by NRB, whether they are implementing NRB’s directive perfectively or not is very important.

Basically, research methodologies here signifies the research design, sources of data, data collection technique, data collection methods and tools and techniques employed etc. for this purpose descriptive cum analytical research design was adopted. Out of total population of twenty-six commercial banks, two banks are taken as sample using judgmental sampling method. Here two major banks SCBL and Nabil bank is selected from private sector banks. Annual reports and other publications from the basis of secondary data are used. Besides this newspaper, relevant thesis, journals, articles, related websites etc are also used for this research. The data collected from various sources are recorded systematically and presented in the appropriate forms of the tables, charts and appropriate mathematical, statistical, financial, graphical tools have been applied to analyze the data. The data of the five consecutive years of selected banks have analyzed to meet the objectives of the study.

5.2 Conclusion

From the study of various variables like NPL, LLP, Total Loan and Advances, Total Deposit, Net profit and their relation with each other in the form of ratio, correlation and trend has shown satisfactory performance of two banks.

From the ratio analysis and trend analysis Nabil Bank's performance is better than SCBL. NPL level to total loan and advances and total deposit of Nabil bank is declining sharply and faster than SCBL, even though average Total Loan and advances of Nabil is higher than SCBL's.

Trend also reveals higher performance of Nabil than SCBL. The trend of net profit is increasing in higher ratio of Nabil than SCBL's. The trend of NPL of Nabil is negative or virtually there will not be any NPL of Nabil from 2009 onwards. But the trend of SCBL is positive even till 2014.

Borrowing deposit from individuals in the form of various accounts and lending in the form of loan and advances is major function of commercial banks. Besides this role of commercial bank is increasing as the globalization has increased. While disbursing loan and advance to lenders banks have to face various risks. Some lenders may go bankrupt and some may not pay with ill intention. So bank has to face both situations. Because of any reason NPL of Bank will increase. This also increases LLP. According to the categorized as Pass Loan, Doubtful loan and Bad Loan.

Both the private banks under study, SCBL and Nabil, are trying hard to reduce the amount of NPL and LLP. Increase in NPL has two way adverse effects in the performance of bank. First of all Banks have to deposit LLP as compensation and guarantee. This reduces the fund of bank for investment in some profitable sector. In second case it reduces the credibility and accountability of management which could have long term adverse consequences to the bank. The summary can be divided in three different chapter to explain more about it.

5.3 Recommendation

On the basis of findings and analysis following recommendation are proposed to both banks to perform better:

- NPL erodes the performance of commercial banks. It reduces profitability because of LLP. This LLP will reduce banks fund for productive sector. NPL of both are declining so banks have to make every effort to continue this trend.
- Lending loan and advance to various lenders is major function of commercial banks. But SCBL has not lent its deposit as loan and advances in compare to Nabil. SCBL can increase the lending proportion so that the profit of the bank may increase.
- In the spite of Higher Loan and Advances of Nabil than SCBL, the average Net profit is lower than SCBL. So Nabil has to increase net profit by maintaining with the increment with the Loan and Advances.
- The main factors which lead to NPL and improper credit appraisal system, ineffective credit monitoring and supervision system etc. besides that negligence in taking information from Credit Information Bureau may also lead to bad debts. Hence all banks are recommended to be more careful and realistic while granting loan and advances. After advancing loan there should be regular supervision and follow up for proper utilization of loan.
- Trend analysis shows that the Loan and Advance amount of Nabil will increase in future so bank has to train its employee to make efficient and professional in credit appraisal, monitoring and proper risk management.
- Banks have to adhere to the guideline of central bank to reduce the amount of NPL and also to increase accountability and credibility of bank.

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ANNEXURE

Annex-1

Correlation between Loan Loss Provision and Total Loan and Advances of SCBL

LLP(X)	Total Loan and Advances (Y)	XY	X^2	Y^2
78	8143	635154	6084	66308449
71	8935	634385	5041	79834225
88	10790	949520	7744	116424100
69	13719	946611	4761	18821096
56	13680	766080	3136	187142400
Here				
$\sum X=362$	$\sum Y=55267$	$\sum XY=3360850$	$\sum X^2=26766$	$\sum Y^2=637920135$

Correlation coefficient(r) $=\frac{n\sum XY-\sum X.\sum Y}{\sqrt{n\sum X^2-(\sum X)^2}\sqrt{n\sum Y^2-(\sum Y)^2}}$

Correlation coefficient(r) $=\frac{5\times3360850-362\times55267}{\sqrt{5\times26766-(362)^2}\sqrt{5\times637920135-(55267)^2}}$

r = -0.52

P.E(r) $=0.6745\times\frac{1-r2}{\sqrt{n}}$

P.E =0.22

and 6P.E.(r) =1.32

Annex-2

Correlation between Loan Loss Provision and Total Loan and Advances of Nabil Bank

LLP (X)	NPL (Y)	XY	X^2	Y^2
61	10947	667767	3721	119836809
56	13279	743624	3136	176331841
65	15903	1033695	4225	252905409
64	21365	1367360	4096	456463225
45	27590	1241550	2025	761208100
Here				
$\sum X=291$	$\sum Y=89084$	$\sum XY=5053996$	$\sum X^2=17203$	$\sum Y^2=1766745384$

Correlation coefficient(r) $=\frac{n\sum XY-\sum X.\sum Y}{\sqrt{n\sum X^2-(\sum X)^2}\sqrt{n\sum Y^2-(\sum Y)^2}}$

Correlation coefficient(r) $=\frac{5\times5053996-291\times89084}{\sqrt{5\times17203-(291)^2}\sqrt{5\times1766745384-(89084)^2}}$

r =-0.063

P.E(r) $=0.6745\times\frac{1-r^2}{\sqrt{n}}$

P.E =0.3004

& 6P.E=1.802

Annex-3

Correlation between LLP and NPL of SCBL

LLP(X)	**NPL (Y)**	**XY**	**X^2**	**Y^2**
78	226	17628	6084	51076
71	196	13916	5041	38416
88	197	17336	7744	38809
69	129	8901	4761	16641
56	123	6888	3136	1529
Here,				
∑X=362	∑Y=871	∑XY=64669	∑X2=26766	∑Y2=160071

Correlation coefficient(r) $= \frac{n\sum XY - \sum X.\sum Y}{\sqrt{n\sum X^2 - (\sum X)^2}\sqrt{n\sum Y^2 - (\sum Y)^2}}$

Correlation coefficient(r) $= \frac{5 \times 64669 - 362 \times 871}{\sqrt{5 \times 26766 - (362)^2}\sqrt{5 \times 160071 - (871)^2}}$

r=0.746

P.E(r)=0.6745×$\frac{1-r2}{\sqrt{n}}$

& 6P.E(r)=0.803

Annex-4

Correlation Between LLP of NPL of Nabil

LLP (X)	NPL (Y)	XY	X^2	Y^2
61	245	14945	3721	60025
56	183	10248	3136	33489
65	178	11570	4225	31684
64	171	10944	4096	29241
45	159	7155	2025	25281
Here,				
$\sum X=291$	$\sum Y=936$	$\sum XY=54062$	$\sum X^2=17203$	$\sum Y^2=179720$

Correlation coefficient(r) $=\frac{n\sum XY-\sum X.\sum Y}{\sqrt{n\sum X^2-(\sum X)^2}\sqrt{n\sum Y^2-(\sum Y)^2}}$

Correlation coefficient(r) = $\frac{5\times54062-291\times936}{\sqrt{5\times17203-(291)^2}\times\sqrt{5\times179720-(936)^2}}$

r= 0.353

P.E(r) = $0.6745\times\frac{1-r2}{\sqrt{n}}$

P.E. r =0.264

& 6P.E =0.1.584

Annex-5

Correlation between Total Loan and Advances and Total Deposit of SCBL

Total Loan and Advances (X)	Total deposit (Y)	XY	X^2	Y^2
8143	19364	157681052	66308449	374964496
8935	23061	206050035	79834225	531809721
10790	24640	265865600	116424100	607129600
13719	24640	265865600	188210961	884646049
13680	35871	490715280	187142400	1286728641
Here,				
$\sum X$=55267	$\sum Y$=132679	$\sum XY$=1528356184	$\sum X^2$=637920135	$\sum Y^2$=3685278507

Correlation coefficient(r) = $\frac{n\sum XY-\sum X.\sum Y}{\sqrt{n\sum X^2-(\sum X)^2}\sqrt{n\sum Y^2-(\sum Y)^2}}$

Correlation coefficient (r)

$=\frac{5\times1528356184-55267\times132679}{\sqrt{5\times637920135-(55267)^2}\times\sqrt{5\times3685278507-(132679)^2}}$

r =0.927

P.E(r)=0.6745×$\frac{1-r2}{\sqrt{n}}$

P.E. r= 0.424

&6P.E =0.255

Annex-6

Correlation between Total Loan and Advances and Total Deposit of Nabil

Total loan and Advances (X)	**Total Deposit (Y)**	**XY**	**X^2**	**Y^2**
10947	14587	159683889	119836809	212780569
13279	19347	256908813	176331841	374306409
15903	23342	371207826	252905409	544848964
21365	31915	681863975	456463225	1018567225
27590	37348	1030431320	761208100	1394873104
Here,				
$\sum X$=89084	$\sum Y$=126539	$\sum XY$=1500095823	$\sum X^2$=1766745384	$\sum Y^2$=3545376271

Correlation coefficient(r) = $\frac{n\sum XY - \sum X.\sum Y}{\sqrt{n\sum X^2 - (\sum X)^2}\sqrt{n\sum Y^2 - (\sum Y)^2}}$

Correlation coefficient r

$$= \frac{5 \times 1500095823 - 89084 \times 126539}{\sqrt{5 \times 1766745384 - (89084)^2} \times \sqrt{5 \times 3545376271 - (126539)^2}}$$

r=0.989

P.E(r) = $0.6745 \times \frac{1 - r2}{\sqrt{n}}$

P.E. r =0.0066

& 6P.E r =0.04

Annex-7

Trend of Total Loan Loss provision of SCBL

Year X	Loan Loss Provision (Y)	X^2	Y^2
1	78	1	78
2	71	4	142
3	88	9	264
4	69	16	276
5	56	25	276
$\sum X=15$	$\sum Y=362$	$\sum X^2=55$	$\sum XY=1040$

Here,

$\sum Y=na+b\sum X$…………2

$\sum XY=a\sum X+b\sum X^2$…….3

A=86.2

B=-4.6

Year	Estimated Loan Loss Provision
2010	58.6
2011	54
2012	49.4
2013	44.8
2014	40.2

Annex-8

Trend of Total Loan Loss Provision of Nabil Bank

Year X	LLP(Y)	X^2	XY
1	61	1	61
2	56	4	112
3	65	9	195
4	64	16	356
5	45	25	225
$\sum X=15$	$\sum Y=291$	$\sum X^2=55$	$\sum XY=849$

Here,

$\sum Y=na+b\sum X$…………2

$\sum XY=a\sum X+b\sum X^2$…….3

A=65.4

B=-2.4

Year	Estimated Loan Loss Provision
2010	51
2011	48.6
2012	46.2
2013	43.8
2014	41.4

Annex-9

Trend of NPL of SCBL

Year(X)	NPL(Y)	X^2	XY
1	226	1	226
2	196	4	392
3	197	9	591
4	129	16	516
5	123	25	615
$\sum X=15$	$\sum Y=871$	$\sum X^2=55$	$\sum XY= 2340$

Here,

$\sum Y=na+b\sum X$…………2

$\sum XY=a\sum X+b\sum X^2$……….3

A= 256.1

B=- 27.3

Year	Estimated NPL
2010	92.3
2011	65
2012	37.7
2013	10.4
2014	-16.9

Annex-10

Trend of NPL of Nabil Bank

Year (X)	**NPL (Y)**	**X^2**	**XY**
1	245	1	245
2	183	4	366
3	178	9	534
4	171	16	684
5	159	25	795
$\sum X=15$	$\sum Y=936$	$\sum X^2=55$	$\sum XY=2624$

Here,

$\sum Y = na+b\sum X$…………2

$\sum XY = a\sum X+b\sum X^2$……….3

A = 242.4

B =-18.4

Year	**Estimated NPL**
2010	132
2011	113.6
2012	95.2
2013	76.8
2014	58.4

Annex-11

Trend Analysis of Net- Profit of SCBL

Year X	Net-Profit Y	X^2	XY
1	536	1	536
2	659	4	1318
3	692	9	2076
4	819	16	3276
5	1025	25	5125
$\sum X=15$	$\sum Y=3731$	$\sum X^2=55$	$\sum XY=12331$

Here,

$\sum Y$ = na+b ...………2

$\sum XY = a\sum X+b\sum X^2$……….3

A = 404.8

B =113.8

Year	Estimated NPL
2010	1087.6
2011	1201.4
2012	1315.2
2013	1429
2014	1542.8

Annex-12

Trend Analysis of Net-Profit of Nabil Bank

Year X	Net-Profit Y	X^2	XY
1	550	1	550
2	665	4	1330
3	673	9	2019
4	764	16	3056
5	1031	25	5155
$\sum X=15$	$\sum Y=3683$	$\sum X^2=55$	$\sum XY=12110$

Here,

$\sum Y = na+b\sum X$…………2

$\sum XY = a\sum X+b\sum X^2$……….3

A = 418.3

B =106.1

Year	Estimated NPL
2010	1054.9
2011	1161
2012	1267.1
2013	1373.2
2014	1479.3

Annex-13

Trend Analysis of Total Loan and Advances of SCBL

Year X	Total Loan and Advances (Y)	X^2	XY
1	8143	1	8143
2	8935	4	17870
3	10790	9	32370
4	13719	16	54876
5	13680	25	68400
$\sum X=15$	$\sum Y=55267$	$\sum X^2=55$	$\sum XY=181659$

Here,

$\sum Y = na+b\sum X$…………2

$\sum XY = a\sum X+b\sum X^2$……….3

A = 6296

B =1585.8

Year	Estimated NPL
2010	15810.8
2011	17396.6
2012	18982.4
2013	20568.2
2014	22154

Annex-14

Trend Analysis of Total Loan and Advances of SCBL

Year X	**Total Loan and Advances (Y)**	**X^2**	**XY**
1	10947	1	10947
2	13279	4	26558
3	15903	9	47709
4	21365	16	85480
5	27590	25	85480
$\sum X=15$	$\sum Y=89084$	$\sum X^2=55$	$\sum XY=308624$

Here,

$\sum Y = na+b\sum X$…………1

$\sum XY = a\sum X+b\sum X^2$……….2

A = 5405.2

B =4137.2

Year	**Estimated NPL**
2010	30228.4
2011	34365.6
2012	38502.8
2013	42640
2014	46777.2

Nabil Bank Limited

Profit and Loss Account

For the period of July 16, 2008 to July 15, 2009

(In NPR)

S.N.	Particulars	Schedule	This Year	Previous Year
1.	Interest Income	18	2,798,486,196	1.978.696.727
2.	Interest Expenses	19	1,153,280,052	758,436,212
	Net interest income		**1,645,206,144**	**1,220,260,525**
3.	Commission & Discount	20	179,693,027	159,319,857
4.	Other Operating Income	21	144,164,143	94,359,475
5.	Exchange income	22	251,919,712	196,487,415
	Total Operating Income		**2,220,983,026**	**1,670,427,262**
6.	Staff Expenses	23	339,897,913	262,907,576
7.	Other Operating Expenses	24	265,158,033	220,750,570
8.	Exchange Loan	22	-----------	-----------
	Operating profit before provision for possible losses		**1,615,927,080**	**1,186,769,116**
9.	Provision for possible loan losses	25	45,722,434	64,055,186
	Operating Profit		**1,570,204,646**	**1,122,713,930**
10	Non-operating income/(expense)	26	2,190,102	24,083,737
11.	Provision for possible losses write back	27	10,617,867	11,100,529
	Profit From Regular Activity		**1,626,534,841**	**1,197,889,004**
12.	Income/ (expense) from extra activities	28	43,521,866	39,990,808
	Profit From All Activities		**1,626,534,841**	**1,197,889,004**
13.	Provision for staff bonus		147,866,771	108,899,000
14.	Provision for income tax		447,614,612	342,521,610
	Current tax		470,701,21	340,625,244
	Prior tax		918,745	52,872
	Deferred tax		(24,006,054)	1,843,494
	Net Income/ (Loss)		**1,031,053,054**	**746,468,394**

Standard Chartered Bank Limited

Balance Sheet

As on July 15, 2009

(In NPR)

S.N	Assets	Schedule	This year	Previous Year
1.	Cash Balance	4.8	463,345,996	414,875,467
2.	Balance With NRB	4.9	1,851,132,637	1,266,273,524
3.	Balance with Banks/Financial institutions	4.10	822,684,902	369,094,233
4.	Money at call and short notice	4.11	2,055,549,000	2,197,537,600
5.	Investments	4.12	20,236,121,082	13,718,597,132
6.	Loans, Advances and Bills Purchase	4.13	13,679,756,990	13,718,597,132
7.	Fixed assets	4.14	137,292,540	117,272,258
8.	Non-Banking Assets	4.15	-----------------	----------------
9.	Other assets	4.16	1,341,584,862	1,349,319,111
	Total Assets		**40,587,468,009**	**33,335,788,326**
	Capital & Liabilities	**Schedule**	**This Year**	**Previous Year**
1.	Share Capital	4.1	931,966,400	620,784,000
2.	Reserve and Funds	4.2	2,120,503,331	1,871,763,996
3.	Debentures and Bonds	4.3	-------------	----------------
4.	Loans ans Borrowings	4.4	300,000,000	---------------
5.	Deposit Liability	4.5	35,871,721,127	29,743,998,794
6.	Bills Payables	4.6	72,941,748	87,397,021
7.	Proposed and Unpaid Dividend		476,296,048	506,366,940
8.	Income Tax Liabilities		4,262,601	2,051,550
9.	Other Liabilities	4.7	809,776,754	503,426,025
	Total Capital & Liabilities		**40,587,468,009**	**33,335,788,326**

Standard Chartered Bank Limited

Profit and Loss Account

For the Period of July 16, 2008 to July 15, 2009

(In NPR)

S.N.	Particulars	Schedule	This Year	Previous Year
1.	Interest Income	4.18	1,887,221,257	1,559,195,526
2.	Interest Expenses	4.19	543,786,600	471,729,700
	Net Interest income		**1,343,434,657**	**1,119,465,826**
3.	Commission and Discount	4.20	325,468,846	276,432,255
4.	Other operating income	4.21	33,191,251	32,594,885
5.	Exchange income	4.22	480,030,913	345,653,020
	Total Operating Income		**2,092,125,667**	**1,774,145,186**
6.	Staff expenses	4.23	253,055,504	225,256,195
7.	Other operating expenses	4.24	276,326,674	230,571,409
8.	Exchange loss	4.22	--------------	--------------
	Operating Profit Before Provision For Possible Losses		**1,562,743,489**	**1,318,317,582**
9.	Provision for possible losses	4.25	56,634,631	69,885,338
	Operating Profit		**1,506,108,858**	**1,248,432,249**
10.	Non-operating income/(expense)	4.26	22,098,317	1,682,509
11.	Provision for possible losses write back	4.27	101,075,167	90,634,940
	Profit from Regular Activity		**1,629,282,342**	**1,340,749,693**
12.	Income/(expense) from extraordinary activities	4.28	(15,356,059)	(28,039,437)
	Profit from all activities		**1,613,926,283**	**1,312,710,256**
13.	Provision for staff bonus		146,720,571	119,337,296
14.	**Provision for income tax**		**442,091,176**	**374,451,952**
	Current tax		443,119,138	381,493,368
	Deferred tax		(1,027,962)	(7,041,416)
	Net Profit /(Loss)		**1,025,114,536**	**818,921,008**

Nabil Bank Limited

Balance Sheet

As on 15 July, 2009

(In NPR)

S.N	Assets	Schedule	This Year	Previous Year

1.	Cash Balance	8	674,395,434	511,426,584
2.	Balance with NRB	9	2,648,596,348	1,829,470,769
3.	Balance with banks/financial institutions	10	49,520,689	330,243,702
4.	Money at call & shot notice	11	552,888,297	1,952,360,700
5.	Investments	12	10,826,379,001	9,939,771,428
6.	Loans, Advances & Bills Purchase	13	27,589,933,041	21,365,053,318
7.	Fixed Assets	14	660,988,986	598,038,998
8.	Non banking assets	15	--------	-----------
9.	Other assets	16	864,695,708	606,393,650
	Total Assets		**43,867,397,504**	**37,132,759,149**
S.N	**Capital & Liabilities**	**Schedule**	**This Year**	**Previous Year**
1.	Share capital	1	965,747,000	689,216,000
2.	Reserve and Surplus	2	164,593,637	1,747,983,989
3.	Debentures and bonds	3	300,000,000	240,000,000
4.	Borrowings	4	1,681,305,00	1,360,000,000
5.	Deposits	5	37,348,255,840	31,915,047,4676
6.	Bills payable	6	463,138,615	238,421,890
7.	Proposed & unclaimed dividend		361,325,024	437,373,004
8.	Income tax liabilities		80,232,454	38,776,869
9.	Other liabilities	7	502,899,934	465,940,930
	Total Capital & Liabilities		**43,867,397,504**	**37,132,759,149**