

**A STUDY ON LENDING PRACTICES
OF
FINANCE COMPANIES IN NEPAL**
(With Special Reference to five Finance Companies)

By :

Sumita Bhatta

Shanker Dev Campus

T.U. Registration No: 7-2-271-242-2003

Campus Roll No: 137/ 2063

A Thesis

Submitted to:

Office of the Dean

Faculty of Management

Tribhuvan University

*In the partial fulfillment of the requirements of
Masters of Business Studies (M.B.S)*

Kathmandu

April 2010

DECLARATION

I hereby declare that the work reported in this thesis entitled “**Lending Practices of Finance Companies in Nepal (With Special Reference to Five Finance Companies)**”, submitted to Shanker Dev Campus, Faculty of Management, Tribhuvan University, is my original work done in the form of partial fulfillment of the requirement for the Masters of Business Studies (MBS) under the supervision of Dr.Kamal Das Manandhar, of Shanker Dev Campus.

Date:

Sunita Bhatta

(Researcher)

Shankar Dev Campus

Redg. No: 7-2-271-242-2003

Roll No: 137/ 2063

Acknowledgement

This Thesis entitled "Lending Practices of Finance Companies in Nepal (With Special Reference to Five Finance Companies)" has been completed under the supervision of Dr. Manohar Krishna Shrestha, Shanker Dev Campus. This thesis provides knowledge about the lending practices of finance companies.

After some period of research, investigation, data collection, analysis and Classification it has now been favourable to interpret into a thesis form.

Thanks to the "Dr.Kamal Das Manandhar of Shanker Dev Campus"for devoting his valuable time and providing guidance throughout the project for writing and rectifying the report .This project had really made me confident and had given me practical approach to various situations.

Each page of this thesis reflects my determination along with the support of the organization to overcome complexities. This thesis is prepared after the hard work, dedication and the all the support from the people related with this thesis.

Finally I would like thank all those kind people who had helped me directly or indirectly in giving the final looks to this thesis.

*Thank you,
Sunita*

TABLE OF CONTENTS

	Page No.
RECOMMENDATION	
VIVA VOCE SHEET	
DECLARATION	
ACKNOWLEDGEMENT	
TABLE OF CONTENTS	
LIST OF TABLES	
LIST OF FIGURES	
ABBREVIATIONS	
CHAPTER I INTRODUCTION	1-20
1.1 General Background	1
1.2 History of Finance Company	13
1.3 Statement of the Problem	16
1.4 Objectives of the Study	17
1.5 Importance of the Study	18
1.6 Limitations of the Study	19
1.7 Organization of the Study	20
CHAPTER II REVIEW OF LITERATURE	21-44
2.1 Review of Relevant Studies	21
2.1.1 Conceptual / theoretical review	21
2.1.2 Review of Journals	24
2.1.3 Review of Relevant NRB Directives	33
2.1.4 Review of Unpublished Desertions	41
CHAPTER III RESEARCH METHODOLOGY	45-55
3.1 Research Design	46
3.1.1 Source of Data	47
3.1.2 Population and Sample	48
3.1.3 Data Collection Procedures	48
3.2 Analysis of Data	48
3.2.1 Financial Tools	48
3.2.2 Statistical Tools	50

3.2.3 Qualitative Analysis	55
Chapter IV PRESENTATION AND ANALYSIS	56-89
4.1 Measuring the Lending Strength	56
4.1.1 Measuring the Lending Strength in Relative Terms	56
4.1.1.1 Investment to Loans and Advances and Investment Ratio	56
4.1.1.2 Loans and Advances and Investment to Total Deposit Ratio	57
4.1.1.3 Loans and Advances to Shareholder's Equity Ratio	59
4.1.2 Measuring the Lending Strength in Absolute Terms	60
4.1.2.1 Loans and Advances	60
4.1.2.2 Non-Performing Loan	61
4.1.2.3 Interest Income from Loans and Advances	63
4.1.2.4 Loan Loss Provision	64
4.1.2.5 Net Profit	66
4.2 Analyzing the portfolio behaviors of Loans & Advances	68
4.2.1 Category wise Loan Classification	68
4.2.2 Performing Loan to Total Loan and Advances Ratio (%)	71
4.2.3 Non Performing Loan to Total Loan and Advances Ratio	71
4.3 Analyzing the Lending Efficiency and its contribution in Total Profitability	72
4.3.1 Loan Loss Provision to Total Loans and Advances Ratio	72
4.3.2 Non-Performing Loans to Total Loan and Advances Ratio	73
4.3.3 Interest Income from Loans and Advances to Total Income Ratio	74
4.3.4 Loans and Advances and Investment to Total Deposit Ratio	75
4.3.5 Interest Income to Interest Expenses Ratio	76
4.3.6 Net Profit to Shareholder's Equity Ratio	77
4.3.7 Earning Per Share (EPS)	77
4.4 Measuring Correlation between Different Variables	78
4.4.1 Correlation between Deposits and Loans and Advances	78
4.4.2 Correlation between ShareHolder's Equity and Loans & Advances	79

4.4.3 Correlation between Investments and Loans & Advances	80
4.4.4 Correlation between Total Income and Loans and Advances	81
4.4.5 Correlation between Loan Loss Provision and Loans & Advances	82
4.4.6 Correlation between Interest Income and Net Profit	83
4.5 Measuring Regression of one variable on the other	83
4.5.1 Regression Analysis of Loans and Advances on Deposit	84
4.5.2 Regression Analysis of LLP on Loans and Advances	84
4.6 Measuring the Propensity of Growth based on Trend Value	85
4.6.1 Trend analysis and Propensity of Growth of Loans and Advances	86
4.6.2 Trend analysis and Propensity of Growth of Earning Per Share	87
4.7 Qualitative analysis of Recovery of Loan	88
Chapter V	
SUMMARY, FINDINGS, CONCLUSION AND RECOMMENDATION	90-95
5.1 Summary	90
5.2 Findings and Conclusion	91
5.3 Recommendation	95
BIBLIOGRAPHY	
APPENDIX	

Table of Contents

APPROVAL SHEET

RECOMMENDATION

DECLARATION

ACKNOWLEDGEMENT

LIST OF TABLES

LIST OF CHARTS

Chapter I INTRODUCTION	1
1.1 General Background	1
1.2 History of Finance Company	14
1.3 Statement of Problem	16
1.4 Objectives of the Study	18
1.5 Importance of the Study	19
1.6 Limitations of the Study	19
1.7 Organization of the Study	20
Chapter II REVIEW OF LITERATURE	21
2.1 Review of Relevant Studies	21
2.1.1 Conceptual framework	21
2.1.2 Review of Journals	24
2.1.3 Review of Relevant NRB Directives	33
2.1.4 Review of Unpublished Dissertations	41
Chapter III RESEARCH METHODOLOGY	44
2.2 Research Design	44
2.2.1 Source of Data	46
2.2.2 Population and Sample	47
2.2.3 Data Collection Procedure	47
2.3 Analysis of Data	47
2.3.1 Financial Tools	41
2.3.2 Statistical Tools	49
2.3.3 Qualitative Analysis	54
Chapter IV PRESENTATION AND ANALYSIS	73

3.1 Measuring the Lending Strength	73
3.1.1 Measuring the Lending Strength in Relative Terms	73
3.1.1.1 Investment to Loans and Advances and Investment Ratio	73
3.1.1.2 Loans and Advances and investment to Total Deposit Ratio	75
3.1.1.3 Loans and Advances to Shareholder's Equity Ratio	76
3.1.2 Measuring the Lending Strength in Absolute Terms	77
3.1.2.1 Loans and Advances	78
3.1.2.2 Non-Performing Loans	79
3.1.2.3 Interest Income from Loans and Advances	82
3.1.2.4 Loan Loss Provision	83
3.1.2.5 Net Profit	85
3.2 Analyzing the Portfolio Behavior of Loans and Advances	87
3.2.1 Category wise Loan Classification	87
3.2.2 Hire Purchase Loan to Total Loan and Advances Ratio (%)	92
3.2.3 Housing Loan to Total Loan and Advances Ratio (%)	93
3.2.4 Term Loan to Total Loan and Advances Ratio (%)	94
3.3 Analyzing the Lending Efficiency and its contribution to Total Profitability	95
3.3.1 Loan Loss Provision to Total Loan & Advances Ratio	95
3.3.2 Non-Performing Loans to Total Loan and Advances Ratio	96
3.3.3 Interest Income from Loans and Advances to Total Income Ratio	98
3.3.4 Interest Suspense to Total Interest Income from Loans & Advances Ratio	99
3.3.5 Loans and Advances to Total Deposit Ratio	100
3.3.6 Interest Income to Interest Expenses Ratio	101
3.3.7 Net Profit to Shareholder's Equity Ratio	102
3.3.8 Earning Per Share (EPS)	103
3.4 Measuring Correlation Between Different Variables	103
3.4.1 Correlation between Deposits and Loans and Advances	104
3.4.2 Correlation between ShareHolder's Equity and Loans and Advances	105
3.4.3 Correlation between Investments and Loans and Advances	105
3.4.4 Correlation between Total Income and Loans and Advances	107
3.4.5 Correlation between Interest Suspense and Interest Income	107

3.4.6	Correlation between Loan Loss Provision and Loans and Advances	108
3.4.7	Correlation between Interest Income and Net Profit	109
3.5	Measuring Regression of one variable on other	110
3.5.1	Regression Analysis of Loans and Advances on Deposit	110
3.5.2	Regression Analysis of LLP on Loans and Advances	111
3.6	Measuring the Propensity of Growth based on Trend Value	111
3.6.1	Trend Analysis and Propensity to Growth of Loans and Advances	112
3.6.2	Trend Analysis and Propensity to Growth of EPS	113
3.7	Qualitative Analysis of Recovery of Loan	115
Chapter V	SUMMARY, FINDINGS, CONCLUSION AND RECOMMENDATION	117
4.1	Summary	117
4.2	Findings and Conclusion	118
4.3	Recommendation	125
	BIBLIOGRAPHY	
	APPENDIX	

List of Tables

Table no.	Tables	Page
1	Relations of Loans and Advances with Total Deposit and Loan Loss Provision of all finance companies	16
2	Investment to Loans and Advances and Investment Ratio	57
3	Loans and Advances and investment to Total Deposit Ratio	58
4	Loans and Advances to Shareholder's Equity Ratio	59
5	Loans and Advances (in millions)	60
6	Non-Performing Loan (in millions)	62
7	Interest Income from Loans and Advances (in millions)	63
8	Loan Loss Provision (in millions)	65
9	Net Profit (in millions)	67
10	Category wise Loan Classification – Lalitpur Finance Co. (in million)	68
11	Category wise Loan Classification – Lumbini Finance & Leasing Co. (in millions)	69
12	Category wise Loan Classification – People's Finance Ltd. (in million)	69
13	Category wise Loan Classification – Union Finance Co. Ltd. (in million)	70
14	Category wise Loan Classification – NIDC Capital Markets Ltd. (in million)	70
15	Performing Loan to Total Loan and Advances Ratio	71
16	Non Performing Loan to Total Loan and Advances Ratio	71

17	Loan Loss Provision to Total Loan & Advances Ratio	72
18	Non-Performing Loans to Total Loan and Advances Ratio	73
19	Interest Income from Loans and Advances to Total Income	74
20	Loan and Advances and Investment to Total Deposit Ratio	75
21	Interest Income to Interest Expenses Ratio	76
22	Net Profit to Shareholder's Equity Ratio	77
23	Earning Per Share (EPS)	78
24	r, P.Er and 6xP.Er between Deposits and Loans and Advances	79
25	r, P.Er and 6xP.Er between ShareHolder's Equity and Loans and Advances	79
26	r, P.Er and 6xP.Er between Investments and Loans and Advances	80
27	r, P.Er and 6xP.Er between Total Income and Loans and Advances	81
28	r, P.Er and 6xP.Er between Loan Loss Provision and Loans and Advances	82
29	r, P.Er and 6xP.Er between Interest Income and Net Profit	83
30	Regression Equation of Loans and Advances on Deposit	84
31	Regression Equation of LLP on Loans and Advances	85
32	Trend Equation and Propensity to Growth of Loans and Advances (in million)	86
33	Trend Equation and Propensity to Growth of EPS (in million)	87

List of Figures

Chart No.	Charts	Page
1	Loans and Advances	61
2	Non-Performing Loans	62
3	Interest Income from Loans and Advances	64
4	Loan Loss Provision	66
5	Net Profit (in millions)	67
6	Trend Behaviour of EPS	87

ABBREVIATION

BOD	-	Board Of Directors
B.S.	-	Bikram Sambat
Co.	-	Company
C.V.	-	Coefficient of Variance
EPS	-	Earning Per Share
Govt.	-	Government
LLP	-	Loan Loss Provision
Ltd.	-	Limited
NIDC	-	NIDC Capital Markets
NEPSE	-	Nepal Stock Exchange
NPL	-	Non-Performing Loan
NRB	-	Nepal Rastra Bank
PEFIL	-	Peoples Finance Company
P.Er.	-	Probable Error
Pvt.	-	Private
S.D.	-	Standard Deviation