CHAPTER- ONE

INTRODUCTION

1.1. Background of the Study

The role of money in an economy is very important. Proper and well planned management of money directs, determines and enhances the health and productivity of total financial sector and the performance of the financial sector affect the growth of the economy. Hence, money is the subject to manage and banks are the manager thereof. Bank, as a manager collects, disperses and controls the flow of money. Banks collect the fund from public who has savings and disperse the fund to the person who is in need of it. In this way, whole infrastructure of national development, direction of economy, rate of progress and even the habit of people is the functions of banking system. Therefore, the existence of a bank is for the change in every aspect of human beings and its presence is for the uplift of people.

During the early periods, although private individuals mostly did the banking business, many countries established public banks either for the purpose of facilitating commerce or to serve the government. The Bank of Venice, established in 1157, is supposed to be the most ancient bank, which however was not a bank in modern sense. It was simply an office for the transfer of the public debt. Eventually, during 1401, a public bank was established in Barcelona. It used to exchange, receive deposits and discount bill of exchange, both for the citizen and foreigners. Similarly, The Bank of Geneva was established in 1407 and The Bank of Amsterdam was established in 1609. The Bank of Amsterdam was established to meet the needs of merchants of the city. The Bank also adopted a plan by which depositors receive a kind of certificate entitling them to withdraw his deposit within six months. Most of the European existing banks were found on the model of the Bank of Amsterdam.

In Nepal borrowing and lending activity has been recorded long ago however, there was no organized institution for such activity until Malla King Jayasthiti Malla, on the basis of occupation divided the people into 64 categories out of which "Tanka Dhari" was formed. The main occupation of "Tanka Dhari" was to lend money. Then after during Rana regime Prime Minister Ranodip singh established a government institution called "Tejarath Adda." The "Tejarath Adda" helped the public by supplying easy and cheap credit against the security of gold and silver ornaments. But the debt facility was only opened for government officials. The general public has to depend on the private money lenders for the debt who used to charge high interest rate and exploit them.

The advent of financial institution in Nepal started with the establishment of Nepal Bank Limited in Year 1994 B.S. under the "Banking Act 1993." Then after Nepal Rastra Bank, the central bank emerged in 2013 B.S. under "Nepal Rastra Bank Act- 2012" which is apex financial institution providing policies and guidance to the financial sectors on one hand and is monitoring and controlling them on the other hand. Realizing the need of adequate banking services for the integrated and speedy development of industrial sector, Rastriya Banijya Bank (RBB) came into existence in 2022 B.S. (NRB Report, 1987:3).

Economic liberalization policy of the Government has encouraged the establishment and growth of financial institutions in Nepal. Now, there are so many financial institutions (FI) such as commercial banks, development banks, finance companies and cooperatives in operation. Some other institutions in pipeline are supposed to come into function very soon. Before the year 2041 B.S. there were only two commercial banks in existence. As the government owned banks were not able to cater the need of the people with modern banking facilities the need of privately owned banks were badly felt and there was rapid growth of commercial banks during a short span of time. The number of commercial banks, development banks, finance companies, and micro finance development Banks reached 23, 58, 79 and 12 respectively in April 2008. The number of branches of commercial Bank has also reached 596 in mid April 2008 (economic survey F/Y 2007/2008).

Banking sectors are the backbone of a country's economy. Motto of the commercial banks is to mobilize the resources by investing the same in a profitable manner. The resources may include capital funds consisting of shareholders equity, money deposited by the people, borrowings and profit capitalization. The competency of any commercial banks is referred as to the utilization of the resources on most profitable manner. The profit should be adequate to meet its costs of funds as well as there should be some margin left over as the reward for risk bearing. The financial institutions are supposed to have contribution for the economic reforms in the country. Though, their activities are guided by some social obligations, some profit is always desirable for maintaining existence.

A big chunk of resources are being utilized on loan and advances. As the return from loan floatation is higher than the return from any other activities, commercial banks are concentrating their financial activities for the management of loans and advances. By virtue of principle for higher return higher risk should be taken and vice versa. The mushrooming growth of the banks has led them towards cut throat competition among the banks is just to share from the small and same size of the cake.

The less opportunity for getting avenues for loan floatation has compelled the banks to finance without being choosy. Quality of the loans and advances could not be maintained to the desirable level if there is no choice whether to finance or not. Once the loan is given it is supposed that the re-payment of interest or principle have to be served without any hindrance. The resources could not be considered utilized properly when the loans provided to the clients could not be regular and if there is cumulative overdue outstanding. There may be various reasons behind the loans that turn irregular from regular one. The main reason may be economic situation of the country, which has global and far- reaching impact. The smooth operation of the commercial banks is possible only when the economy of the country functions well. Satisfactory level of return on investment is the pre-requisite for the financial sector to be groomed. The other contributing factors that turn the good loan into bad are the attitude of the borrower, types and quality of security taken and legal hurdles created by the borrower when the recovery action is started. Once the distributed loan is not returned timely by clients and becomes overdue than it is known as Non-performing assets (NPA) for the banks. Reduction of NPA has always been a significant problem for every commercial banks and proper attention for the management of the NPA now under top priority. Due to various hurdles on way of management of NPA, commercial banks are now losing their profitability and struggling for their existence.

The operations of the banking institution has been regulated by the international norms, relevant acts, regulations, 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. Like wise the expectation of the stakeholder should also be taken into consideration. All banking institutions are supposed to confine their activities within that periphery.

1.2. Bank Overview

The oldest bank of Nepal, Nepal Bank Limited (NBL) was established on 1994 B.S. Kartik 30, Monday (November 15, 1937). NBL's authorized capital was Rs.10 million & issued capital Rs.2.5 million of which paid-up capital was Rs.842 thousand with 10 shareholders. It is the first bank of Nepal to establish under the principle of Joint venture (Joint venture between government and general public).

The vision of the bank is "To remain the leading financial institution of the country." It's Mission is “To provide an environment within which the bank can bring unique financial value and services to all customers." It will be a sound institution where depositors have continuous faith in the security of their funds and receive reasonable returns; borrowers are assured of appropriate credit facilities at reasonable prices; other service - seekers receive prompt and attentive service at reasonable cost; employees are paid adequate compensation with professional career growth opportunities and stockholders receive satisfactory return for their investment. The values of this bank are based on: Respect, Service and Safety for the customers. We serve respect, reward and opportunity for the people with whom we work. Respect, cooperation and support for the economic community of Nepal. The objectives of Nepal Bank Limited are to continue to maintain leading share of banking sector with a significant presence in all major geographical areas in the country, to provide competitive and customer oriented banking services to all customers through competent and professional staff and to reclaim leadership within the national financial community.

1.3. Statement of the Problem

While floating the loans bank expects that interest and principal will be served on time. In principle, loans and advances extended by banks are repayable on demand. But in practice all loans are not recovered as per the terms of sanction or within the expiry of repayment period granted in normal courses. When the interest and principal cannot be recovered in time, the loan is considered as Non Performing Assets (NPA). In the recent days not only government owned banks but some of the banks under private sectors are also suffering from NPA burden. It is a matter of debate among the banking sector regarding the real cause of NPA increment and on some occasion it is said the newly issued NRB directives is the cause of NPA increment. This study has identified the following research questions regarding to NPA with special reference to Nepal Bank Limited.

i) What is the present condition of NPA?
ii) What is the impact of NPA on profitability?
iii) What is the relationship of NPA and total loan and advances?

What is the trend of total deposits, total loan and advances, non performing assets and loan loss provision of NBL?

1.4. Objective of the Study

Non-Performing Assets is a major issue for every commercial bank. Every bank has now put the Non-Performing Assets management under top priority. Thus, in present context, analyzing the cause and implication of NPA obviously shall be useful for banking sector. The basic objective of this study is to analyze and identify the impact, cause and consequences of NPA in Nepal Bank Limited. The basic objectives of this study are as follows:

i) To analyze the present condition of NPA on NBL.
ii) To evaluate the impact of NPA on profitability of the bank.
iii) To assess the relationship of NPA with total loan and advances.
iv) To analyze the trend of total deposits, loan and advances, non-performing assets and loan loss provision of NBL.

1.5. Significance of the Study

NPA may be defined broadly as the bad debt. However NPA in terms of banking sector consists of those loans and advances which are not performing well and likely to be turn as bad loan. NPA has several impacts on the financial institution. On the one hand, the investment becomes worthless as expected return can not be realized and on the other, due to the provisioning required for the risk mitigation, the profitability is directly affected. The existence of the bank can be questioned on this situation. Thus interest along with principle has to be recovered timely and without any obstacles.

Every bank and financial institution (FI) should have categorized their loan and advances under the aging basis as per NRB directives. NRB has directed to maintain loan loss provisioning according to aging basis for risk mitigation. The loan loss provision is to be maintained by debiting profit & loss account. Thus as the quality of loan degrades the ratio of loan loss provision is increased affecting the profitability of the banks. This study will have effort to find out the relationship of NPA on profitability of Nepal Bank Limited.

Management of NPA has led the banks towards the rigorous recovery action, which ultimately may cause auctioning of the security held with bank’s custody. Due to adverse economic situation of the country and perception build up among the people that the properties under auction are always over evaluated, there is less participation of the bidder during auction. Such situation compels the banks to accept the security on its own name. Continuous acceptance of the ownership has now created another problem by piling up the volume of non banking assets (NBA). As the major chunk of NBA are fixed in nature the fund supposed to be rolled over are being tied of on fixed asset, which is heating the liquidity of the banks.

It is confined to analyze the repercussion of NPA on the profitability of the banks. Further it will be an effort to assess the relationship of NPA and NBA. Credit concentration risk and its implication on NPA increment shall also be considered. Affecting internal and external factors for the conversion of NPA shall be another area to be intended to focus under this study. For the analysis of cause and consequences, the NPA level of Nepal Bank Limited shall be taken into consideration.

The Financial Sector Reform Program (FSRP) is in operation in order to make the financial system healthier and efficient. It was launched to improve the financial position along with steer the managerial reform of two state-owned commercial banks (CB) namely Nepal Bank Limited and Rastriya Banijya Bank in November 2000. Under the FSRP, the management of NBL was handed over to a team of ICC

Consulting Group from Bank of Scotland (Ireland) from July 22, 2002 to July 22, 2007.

Problem due to increasing NPA is more or less being faced by every commercial bank in Nepal. To the extent, the nature of problem is similar on every bank. As this problem has already been recognized as serious problem this study will obviously have significant contribution to investigate the issues more systematically. This study will give academic as well as practical significance for the banking industry to identify and trace the contributing factors causing NPA and to reduce its level.

1.6. Limitation of the Study

This study is the search in the NPA problems and its solutions in Nepalese financial sector. The main limitations of the study are as follows:

i) The study is based on the secondary data, so the reliability of the study depends largely upon the reliability of the secondary data.
ii) Cross sectional data are the major limitation to find the casual linkage between NPA and profitability.
iii) This paper is confined to the NPA of Nepal Bank Limited only.
iv) The study covers the period from 2002/2003 to 2006/2007 for the analysis of data.
v) This research used selected tools and technique.
vi) There is time and resource constraint.

1.7. Chapter Scheme of the Study

The research has been carried out for the partial fulfillment of the requirements for the degree of master of business studies (MBS). The research report is organized under the prescribed format by Central Department of Management, Tribhuvan University. The study has been organized into the following five different chapters:

i) **Introduction:** This chapter includes Bank's overview, statement of the problem, background, objective, significant, limitation and chapter scheme of the study.

ii) **Review of literature:** This chapter includes conceptual review and review of related studies.

iii) **Research Methodology:** This chapter includes introduction of research, research design, data collection technique, method of data analysis and tools used for analysis of data

iv) **Analysis and Presentation of Data:** This chapter includes introduction, ratio analysis, correlation analysis and trend analysis.

v) **Summary, Conclusion and Recommendations:** Lastly summary, conclusion and recommendation of the study is given in this chapter.

CHAPTER - TWO

REVIEW OF LITERATURE

The purpose of reviewing the literature is to develop some expertise in one's area, to see what new contribution can be made and to receive some ideas for developing a research design. Thus, the previous studies can't be ignored because they provide the foundation to the present study. In other words, there has to be continuity in research. This continuity in research is ensured by linking the present study with the past research studies. From this, it is clear that the purpose of literature review is to find out what research studies have been conducted in one's chosen field of study and what to be done.

The review of literature is a crucial aspect because it denotes planning of the study. The main purpose of literature review is to find out what works have been done in the area of the research problem under study and what has not been done in the field of the research study being undertaken. For review study, the researcher uses different books, reports, journals and research studies published by various institutions, unpublished dissertations submitted by master level students have been reviewed.

2.1 Conceptual Review

This chapter includes the brief presentation of the origin and concept of bank, Concept of commercial bank, evolution of the banking sector in Nepal with detail profile about the Nepal Bank Limited. This chapter covers the review of theoretical background being implemented as for the management of NPA.

Nepalese commercial banks have now started to give proper attention on NPA. Some banks have recently introduced the NPA management policy for the recovery and regularization of the dues. But relating to the cause of NPA growth and its total impact on financial position of the banks has not been studied so far in detail. There are some articles in this perspective that comes occasionally however those are also not specific for tracing out the cause and effect on NPA.

In India State Bank Staff College, Distance Learning Department, Hyderabad had prepared the paper for the management of NPA which was basically for the purpose of internal management of NPA. No previous research papers have been found in this sector. However, it is tried the best to give the introduction of NPA and categorization norms in India and Nepal through Reserve Bank of India's (RBI) guide line and NRB directives on country specific. For some theoretical aspect some banking related books have also been studied for the assessment of banking approach towards NPA.

2.1.1 Origin of Bank

There are different opinions on the origin of the bank. According to one opinion, the term bank was originated form Italian word 'Banco' which meant bench. The money exchangers at that time kept heap of money on the bench from which came the use of word 'Banco'. In the opinion of Macleod, since banco means 'heap', it denotes the joint fund contributed by many persons.

The origin of the word 'Bank' is linked to:
German word 'Bank' means a joint stock company,
Latin word 'Bank' means a bench,
Italian word 'Bank' means a bench and
French word 'banquet' means a bench (Vaidya, 2001:2).

Moneylenders in the streets of major cities of Europe used benches for acceptance and payment of valuables and coins. When they are unable to meet their liabilities, the depositors used to break their benches. Hence the word 'Bankruptcy' is derived from there (Klise, 1972: 3).

The term bank was first used in Italy in 1157 A.D. in 20th century. The first bank was set up in Venice, Italy as a public bank, by the name 'Bank of Venice'. Subsequently, 'Bank of Barcelona' in 1401 A.D. and 'Bank of Geneva' in 1407 A.D. were established. In 1609 A.D., 'Bank of Amerterdam', a famous bank was established. In reality, the history of modern banking had started from 'Bank of England' in 1694 A.D. But the modern joint stock banks were established in England only in 1833 A.D. In 1844 A.D., 'Banque De France' was established in France in 1807 A.D. Later, the banks were established in other parts of the world (Shekher & Shekher, 1999:2).

2.1.2 Concept of Bank

Generally, an institution established by law, which deals with money & credit is called bank (Bhandari, 2003: 1). It is obvious that in a common sense, an institution involved in monetary transactions is called bank.

A bank is a financial institution, which plays a significant role in the country. It facilitates the growth of trade & industry and boost national economy. However, a bank is a resource of economic development, which maintains the self-confidence of various segments of society and extends credit to the people (Vaidhya, 2001’ 1)

A bank is a business organization that receives and holds deposits of funds from others, makes loans or extends credits & transfers by written orders of depositors (The Encyclopedia America, 1984; 302).

The business of the banking is collection of funds from community & extending credit to people for useful purposes. Bank plays a vital role in making money from lenders to borrowers. Bank is a profit seeking business, not a community charity profit seeker. It is expected to pay dividend & otherwise, add to the wealth of shareholders (Encyclopedia, The world Book, 1984: 6).

Hence, in concise, we can say that there is no single universally accepted definition of bank. In brief, it is an institution, which accepts deposits in different accounts, provides loans of different types, and creates credit.

2.1.3 History of Banking in Nepal

The history of banking in Nepal is not very old. It goes at least back to the Lichchhavi era. There were ‘Gosthies’ to work as credit banks established under the permission of Royal order & they were conducted through local legislation called ‘Panchali’. Then the king Jayasthiti Malla from Malla dynasty, allowed ‘Tankadhari’, a class of people, to deal in depositing & lending of money & ornaments. The Banda who still worked in ornaments used to deal in lending & depositing the ornaments in that time also. Then, the king, Ram Shah played an important role in developing the banking system in Nepal. He found that unorganized lending was taking place in the society at very high interest rates. So, he fixed up the interest rates of lending (Bhandari, 2003: 6).

Though it seemed realizing the development of banking in those early times, it could not be materialized till the end of Rana regime. The first government institutionalized credit house called ‘Tejarath Adda’ was established during the tenure of Prime Minister, Ranoddip Singh (1993 – 1994B.S.). The ‘Tejarath Office’ used to give loans to government employees against the securities of gold, silver, etc (Bhandari, 2003: 7).

Banking, in true sense, started with the inception of Nepal Bank Limited on 30th kartik, 1994 B.S. as the first commercial bank of Nepal. Nepal Bank Limited was established under Nepalese Banking Law & Nepal Bank Act 1994 B.S. formulated by the Industrial Board of Nepal (Bhandari, 2003: 7).

After the Nepal Rastra Bank’s establishment as a central bank on 14th Baisakh, 2013 under Nepal Rastra Bank Act, 2012 B.S., the bank was empowered by the Act to have direct control over banking institution of the country to manage the circulation of national currency along with foreign exchange rate. Then came Rastriya Banijya Bank established on 10th Magh, 2022 B.S. established under Rastriya Banijya Bank Act, 2021 B.S. (Bhandari, 2003: 8).

2.1.4 Concept and Development of Commercial Bank in Nepal

Commercial banks are that financial institutions which deal in accepting deposits of people & institutions & giving loans against securities. They provide working capital needs of trade, industry & even to agricultural sector. Commercial banks also provide technical & administrative assistance to trade, industries & business enterprises. Commercial bank is a corporation, which accepts demand deposits, subject to check & makes short-term loan to business enterprises, regardless of the scope of its other services.

A commercial banker is a dealer in money & substitutes for money, such as cheque or bill of exchange. It also provides a variety of financial services (The New Encyclopedia Britanica, 1985: 605).

The American Institute of Banking has laid down for functions of the commercial banks i.e. receiving & handling deposits, handling payments for its clients, granting loan & investment & creating money by extension of credit (American Institute of Banking, 1985: 609). Principally, commercial banks accept deposits & provide loans, primarily to business firms, thereby facilitating the transfer of funds on the economy (Bhandari, 2003: 65).

In the Nepalese context, a commercial bank is one which exchanges money, deposits money, accepts deposits, grants loans & performs commercial banking functions (Commercial Bank Act, 1974).

Commercial banks are those banks, which pool together the savings of the community & arrange for their productive use. They supply the financial needs of modern business by various means. They accept deposits from the public on the condition that they are repayable on demand of short notice. Commercial banks are restricted to invest their funds in corporate securities. Their business is confined to financing the short-term needs of trade & industry such as working capital financing. They cannot finance in fixed assets. They grant loans in the form of cash, credits & overdrafts. Apart from financing, they also render services like collection of bills & cheques, safe keeping of valuables, financial advising, etc. to their customers (Vaidya, 2001: 38).

In Nepal, 24 commercial banks are operating so far. They are:

1. Nepal Bank Limited
2. Rastriya Banijya Bank
3. Agriculture Development Bank
4. Nabil Bank Limited
5. Standard Chartered Bank Limited
6. Himalayan Bank Limited
7. Nepal Bangladesh Bank Limited
8. Nepal SBI Bank Limited
9. Everest Bank Limited
10. Lumbini Bank Limited
11. Nepal Industrial & Commercial Bank Limited
12. Kumari Bank Limited

13. Nepal Investment Bank Limited
14. Bank of Kathmandu
15. Laxmi Bank Limited
16. Machhapuchhre Bank Limited
17. Nepal Credit & Commercial Bank Limited
18. Siddhartha Bank Limited
19. Global Bank Limited
20. Citizen Bank Limited
21. Sunrise Bank Limited
22. Bank of Asia Limited
23. Development Credit Bank Limited
24. Nepal Merchant Bank Limited

(Source: www. nepalrastrabank.com.np)

The commercial banks in Nepal are categorized into four groups on the basis of capital owned. They are; the fully government owned bank, Rastriya banijya bank, the government and Private sector bank, Nepal Bank Limited and the Joint Venture banks like Nabil Bank Limited, Standard Chartered Bank Limited, Himalayan Bank Limited, Nepal Bangladesh Band Limited etc.

However, central bank is the main bank of any nation that directs & controls all other banks. In Nepal, Nepal Rastra Bank is the central bank & all the commercial bank perform their functions under its rules, regulations & directions.

2.1.5 Functions of Commercial Bank

Commercial banks are the most important types of financial institution for the nation in terms of aggregate assets. Traditional functions of commercial banks are only concerned with accepting deposits & providing loans. But modern commercial banks work for overall development of trade, commerce, services & agriculture also. The business of banking is very broad in modern business age. The number & variety of services provided by bank will probably expand. Recent innovation in banking include the introduction of credit cards, accounting services for business firms, factoring, leasing, participating in the Euro-dollar market & lock-box banking. The main functions of commercial banks are as follows:

i. **Accepting Deposits:** - It is fair deduction that no person or body, corporate or otherwise, can be banker who does not take deposits, issue & pay cheques & collect cheques from his customers. Here, all functions are related with the acceptance of deposits. Therefore, accepting deposits by bank is the oldest function of bank. A bank accepts deposits in three forms viz. saving, current & fixed. Saving deposit is one of the deposits collected form small depositors & low-income depositors. The banks usually pay small interest to depositors for their deposits. Current account is also known as demand deposits. Under this, any amount may be deposited. There are no restrictions regarding number & amount of withdrawals as contrary to saving account. The banks don't pay any interest on such account but charge small amount on the customers having current account. A fixed or time deposit is one where customers are requested to keep a fixed amount in the bank for specific period, generally by those who don't need money for stipulated time. The bank pays a higher interest on such deposits.

ii. **Advancing Loans**: - The second major function of a commercial bank is to provide loans & advances from the money, which it receives by way of deposits for the development of industry, trade, commerce, services & agriculture. The main purpose of commercial bank is to boost up the development pace of communities & the economy as a whole.

iii. **Agency Services:** - The bank also performs number of services on behalf of the customers. The following are the agency functions provided by the bank.

a. Dealing with the transaction of foreign exchange business
b. Serving as an agent of correspondent on behalf of the customers
c. Issuing letter of credit, circulate note, traveler's cheques etc.
d. Purchasing & selling different kinds of securities & remitting funds
e. Keeping valuable article in safe custody
f. Providing financial advice to various persons & bodies whenever required

iv. **Creating Money**: - The major function of the bank that separates it from other financial institution is the ability to create money & to destroy money, which is accomplished by lending & investing activities. The power of the commercial banking is of great economic significant as it results in the elastic credit system that is necessary for the economic progress at a relatively steady growth rate (American Institute of Banking, 1985: 149).

2.1.6 Definition of Loan and Advance

Loan is defined as a thing that is lent, especially a sum of money. Like-wise debt means a sum of money owed to somebody. However in financial terms loan or debt means principal or interest availed to the borrower against the security. Debt means money that bank owes or will lend to individual or person.

Likewise the term loan is defined as a lending. Delivery by one party to and receipt by another party of sum of money upon agreement expressed or implied, to re-pay it with or without interest. Any thing furnished for temporary use to a person at his request, on condition that it shall be returned or it's equivalent in kind, with or without compensation for its use. Loan includes (i) the creation of debt by the lender's payment of or agreement to pay money to the debtor or to a third party for the account of the debtor; (ii) the creation of debt by a credit to an account with the lender upon which the debtor is entitled to draw immediately; (iii) the creation of debt pursuant to a lender credit card or similar arrangement; (iv) the forbearance of debt arising from a loan.

Further debt means 'Principal and Interest provided to debtor by banks or financial institutions, with the pledge of immovable or movable property or other securities or guarantee or without guarantee and the word also means over dues of the transaction beyond balance or fees, commission and interest incurred in that relation (Debt Recovery Act for Bank and Financial Institution, 2058).

2.1.7 Definition of Non-Performing Assets

To define non-performing assets first of all meaning of assets should be understood. Asset means the property of a person or a company. This indicates that assets are the property of a company accumulated with the help of sources.

Non performing loan (NPL) means an outstanding loan that is not repaid, i.e. neither payments on interest or principal are made. In case of the banks, the loan and advance are the assets as the banks flow loans from the funds generated through shareholders equity, money deposited by the people and fund having through the borrowings. Hence, the terms NPA means the loan and advances that are not performing well. Thus, all the irregular loan and advances can be termed as NPA.

2.1.8 Classification of Non-Performing Assets

As per the NRB directives, NPA are said as classified loans. And this includes sub-standard, doubtful and loss categories as defined by new NRB directives. As per the directives, NRB has identified the NPA as an account of loan where the balance sheet date in respect of

- Term loan interest remains "past due" for more than 180 days, overdraft and cash credit account remain out of order,
- Bills purchased or discounted remain overdue or unpaid for more than 180 days,
- Other accounts receivables remain past due for 180 days.

In our country, the previous circular of NRB had classified the loans into six categories; however as per new circular issued and effective from F/Y 2058/2059, commercial banks are required to make provision against loan and advances as follows:

Classification of loans and Advances	**Criteria for provisioning**	**Provisioning rate**
Pass	Non past due and past due for a period up to 3 months (Performing loans)	1%
Substandard	Past due for a period of 3 months to 6 months	25%
Doubtful	Past due for a period of 6 months to 1 year	50%
Loss	Past due for a period of more than 1 year or advance which have least possibility of recovery	100%

However, for F/Y 20058/2059, 2059/2060 and 2060/2061 there are certain relaxation on ageing of due loan. The above criteria are supposed to be effective fully onwards F/Y 2061/2062.

2.1.9 Effect of Non-Performing Assets on Profitability of Bank

Under the circumstances assets that do not earn any income to the bank affect the profits in a number of ways (Athmanathan and Venkatakrishnan, 2001).

Profitability impact

- The resources locked up in NPA are borrowed at a cost and have to earn a minimum return to service this cost.
- NPA on the one hand do not earn any income vu on the other hand drain the profits earned by performing assets through the claim on provisioning requirements.
- Since they do not earn interest, they bring down the yield on advances and the interest margin or the spread.
- NPA have a direct impact on return on assets and return on equity, the two main parameters for measuring profitability of the bank.
- Return on assets will be affected because while the total assets include the NPA they do not contribute to profits, which are the numerator in the ratio.
- Return on equity is also affected as provisioning eats more and more into profits earned.
- The cost of maintaining these assets include administrative costs, legal costs and cost of procuring the resources locked in.
- NPA bring down the profits, affect the shareholder value and thus adversely affect the investor confidence.

As a whole the impact of NPA can be assessed with the following (Athmanathan and Venkatakrishnan, 2001).

- Lower ROE and ROA.
- Lower image and rating of bank.
- Disclosure reduces invertors' confidence.
- Increases costs / difficulties in raising capital.
- NPA do not generate income.
- They require provisioning.
- Borrowing cost of resources locked in.
- Opportunity loss due to non-recycling of funds.

- Capital gets blocked in NPA.
- Utilizes capital but does not generate income to sustain the capital that is locked.
- Recapitalization by government comes with string.
- Administration and recovery cost of NPA.
- Effect on employee morale and decision-making.

2.2 Review of Related Studies

2.2.1 Review of Journals and Articles

On way to conduct this research work some books, journals and publications have been studied to formulate ideas about the subject matter. Although, the specific books regarding the NPA could not be found, however, some banking related books have been consulted such as Tannan's Banking Law and practice in India (1997). Assessing the gravity of the problem, Tannan (1997) found that banks and financial institutions at present face considerable difficulties in recovery of dues from the clients and a significant portion of the funds of banks and financial institutions is thus blocked in unproductive assets.

Likewise for taking reference book on management of bank credit written by Suneja, (1992) has also been consulted. Suneja (1992) pointing out the cause of NPA says that the risk connected with lending to business depends on an enormous number of factors. For any particular type of business the risk failure is affected by the state of economy, trend in demand for the product of service provided, competition from any other suppliers, financial resources are too limited and management skills are lacking. Reiterating the difficulties Suneja (1992) says probably the most difficult decision facing a banker is to determine when it becomes necessary to recall a loan and to begin the process of liquidating the security. Further, she suggests that if a customer fails to make repayment on the due date, the bank has to consider what steps need be taken to recover the debt.

Ghimire (2056) in her article, "Efficiency indicators of commercial bank: A comparative analysis", found that efficiency indicator of the bank may be viewed on the basis of amount allocated for loan loss provisioning against loan and investment.

Basyal (2057) discussing the financial performance of government owned banks in his article “Placing RBB and NBL under management contracts: Rational and Opposition” agreed that the disappointing performance of these two banks has become serious concern to all the stakeholders. Further, he mentions that they are having with huge level of NPA, which could be termed as the darkest sides of their operational inefficiency and undisciplined financial behavior.

Pradhan (2058) in his article “NPA: some suggestions to tackle them” found that unless the growth in NPA is kept in control, it has the potential to cause systematic crisis. He has mentioned that a dream of globalization led to huge investment, which unfortunately could not be utilized properly due to hesitant liberalization policies. Large corporate misused the credits and delayed payments and contributed indirectly for enhancing NPA ratio. He further argues that lack of vision in appraisal of proposal while loan sanctioning, reviewing or enhancing credit limits, absence of risk management policy of financing, concentration of credit in few group of parties and sector, lack of coordination among various financiers, lack of initiatives to take timely action against willful defaulters, indecision on existing out of bad loans for fear of investigating agencies like special police, CIAA, public Accounts Committee of the parliament have also contributed in whatsoever measures to the worsening situation of NPA front. He further pointed out that most crucial reason for the increase in the NPA is the shabby and defaulter friendly legal system. Suggesting the remedy of NPA, he adds that administrative system should be strengthened, legal reforms should be made and Assets Reconstruction Company should be formed.

Bhattarai (2006) in his article of Business Age, it talks about the paper presented by Bhisma Raj Dhungana, Director of NRB. In his paper he has mentioned about the decreasing trend of NPL (Non Performing Loan) in Nepali banking system. The NPL of Nepali banking system is found decreasing though it has not come down to acceptable level (i.e. below 5%). The NPL of banking system was 19% in July 2005 and come down to 13.8% in July 2006. He further elaborates that the foreign management has made wonderful recovery of bad loans in case of RBB, which is one of the two banks contributing significant percentage of NPL, is achieved by writing off significant amount of bad loan, which has ultimately reduced the profit of shareholders. The NPL of RBB has decreased to 45.34% in fourth quarter of the fiscal year 2005/06 from 50.96% in the previous quarter. Similarly, NPL of NBL decreased to 25.11% at the end of fourth quarter from 42.40% in the previous quarter. As per him to reduce the NPL to significant level, financial institution must put in the greater efforts themselves and regulators must be serious to monitor and regulate the market. The writer is hopeful of the current efforts of the Nepal Government to recover the NPL as well as the result of the efforts made by the South East Asian Nations in year 2002. A study of Fungel and Others (2004) showed that China in year 2002, reduced NPL to 20% from the peak level of 42%, Indonesia to 8.1% from peak level 48.6%, Malaysia to 8% from 30.1% and Thailand to 10% from 51.6%. These results were achieved mainly by establishment of Asset Management Companies, initiation of corporate debt restructuring programs, bank capitalization programs and enforcement of bankruptcy law.

In an article published in "The Kathmandu Post" August 28, 2006 on topic "Huge Bank Defaulter: Who is responsible?" Rajub Upadhaya, sr. External Affairs specialist, The World Bank, found saying that defaulters are the villains of the marketplace. The financial sector is suffering due to the defaulters. The most hurt in the situation is the poor. If the defaulting continues, the government will have to spend money from its budget to fix the problems at the expenses of programs that help poor to improve their living standard. Delaying the resolution of the problem will result in accumulation of more losses, eating further into future government resources for poverty reduction.

In an article published in "The Kathmandu Post" August 28, 2006 on topic "Who is responsible? Is Biz community only the culprit?" Arun K. Subedi, Industrialist, printing & packaging, Hetauda found saying that it is the bank's duty to analyze and study the report financially, managerially and technically. If the project is then found to be handsome and having good cash flow then the bankers have to sanction the loan up to the limit of the corporate worth. He complains that bankers bother about collateral only. All policymakers, bankers and the press must know that collateral cannot repatriate the loan. It is the cash flow that repatriates the loan. So, existing investigation and analyses must be concentrated on project status. He is of vies that collateral produces only 60% of the loan if one does not pay loan for more than three years. The same thing happens in project lending; the equity portion will be covered by interest portion of debt. But he has to sign an unethical, illegal and immoral clause of the bond to get loans. They add a clause the right to recover the loan from the individual properties of the promoter's and their family members. A bank is not only the financier but is also the partner of the project when he invests in any project so bankers are equally responsible for the failure of the project. Hence the banks must undertake the project and start to recover the loan by operating and managing. When a project fails, the bankers together with promoters have to sell the properties. If it is inadequate then the banks have to write off the loans instead of claiming unrelated properties of the promoters and should not also blacklist the promoters as they could promote other business. Liabilities of particular company are to be limited to that company.

Though these studies are found to be quite useful in their own side but the question of NPA and its cause as well as effect on various aspects in commercial bank is yet to be reviewed. In view of these, this study gas been based on the various contributing factors that increase NPA level in commercial banks in Nepalese perspective and its effect on profitability position of the banks.

2.2.2 Review of Unpublished Thesis

Niva Shrestha (2004) in her study "A study on non-performing loan and loan loss provisioning of commercial banks" with reference to Nepal Bank Limited, NABIL Bank Limited and Standard Chartered Bank Nepal Limited has made an attempt to analyze the various aspects of non-performing loan in the commercial banks. Her main objective of the study is to find out the proportion of non-performing loan, factors lending to accumulation of non-performing loan, relationship between loan and loan loss provision and impact of loan loss provision on profitability of the commercial bank.

She concludes increasing non-performing loan is the serious problem of the banking sector in Nepal. Non-performing assets directly affects the income flow of the bank. It has been found that NBL has very high portion of non-performing loan resulting to higher portion. Hence, even the bank has the highest investment in the most income generating assets, i.e. loan and advances, it is in loss. Even the private sector banks like NABIL has higher non-performing loan during the study period is higher than the acceptable. However in recent two year, NABIL's non-performing loan has shown significant decrement and according provision has also decreased. Among the three banks SCBNL has the least non-performing loan and thus the least loan loss provision. From these indicators it can be said that SCBNL is the best among the three banks. However SCBNL seems less oriented towards lending. Hence, the lower percentage of NPL and provisioning of SCBNL is not only due to proper lending function but also due to relatively lower investment in loans and advances (Shrestha, 2004: 99).

She also said that ineffective credit policy, political pressure to lend uncreditworthy borrowers, overvaluation of collateral are the major cause of mounting non-performing assets in government owed banks like NBL. Other factors lending to accumulation of NPAs are weak loan sanctioning process, ineffective credit monitoring and supervision system, economic slowdown, borrower's misconduct etc. In addition to this, establishing Recovery Cell, hiring Asset Management Company is also measure to resolve the problem of NPL.

She recommended that the factor which leads to non-performing loan are improper credit appraisal system, ineffective credit monitoring and supervision system etc. Besides that negligence in taking information from credit information bureau may also lead to bad debts. Hence, all the three banks are recommended to be more caution and realistic while granting loan and advances. After advancing loans there should be regular supervision and follow up for proper utilization of loan. It also recommended that the banks to initiate training and development program for the employees to make them efficient and professional in credit appraisal, monitoring and proper risk management. The regulation regarding loan classification and provisioning is stringent and tighter than the previous. Hence NRB should not only impose directives but also create supportive environment for the commercial banks. NRB is recommenced to strength Credit Information Bureau (CIB) so that banks can get required credit information about the borrowers on time. This help in reducing NPL.

Dinesh kumar khadka (2004) in his thesis non-performing assets of Nepalese commercial banks with objectives to examine the level of NPA in total assets, total deposit and total lending of Nepalese commercial banks showed that the effects of nonperforming assets on return on assets and return on equity on Nepalese commercial banks.

He said that despite of being loan and advances more profitable, it creates risk of non-payment for the bank. Such risk is known as credit risk or default risk. Therefore, like other assets, the loan and advances are classified into performing and non-performing assets on the basis of overdue schedule. Escalating level of NPA has been becoming great problem in banking business in the world. In this context, Nepal cannot be run off from such situation. The level of NPA in Nepalese banking business is very alarming. It is well known fact that the problem of swelling non-performing assets (NPA) and the issue is becoming more and more unmanageable day by day. We are well known from different financial reports, newspapers and news that the total NPA in Nepalese banking system is about 35 billion, while it is very worse in case of two largest commercial banks Rastriya Banijaya Bank (RBB) and Nepal Bank Limited (NBL) (Khadka, 2004: 79-82).

Finally, he concludes that the level of NPA in sampled Nepalese commercial banks is not so alarming. The situation is quite satisfactory. But the increasing trend remain continue in coming days, the situation will be unmanageable and alarming. The commercial banks could not give full attention towards supervising their lending and towards recovering their bad loans perfectly. Level of NPA has been increasing. The level of Nepal Bangladesh Bank Limited (NBBL), Nepal SBI bank Limited (NSBIBL) and Bank of Kathmandu limited (BOKL) seems very unsatisfactory. If the situation is not handled right now, it will be unmanageable and difficult to handle.

In other level of NPA of Nepal Investment Bank and NABIL Bank has been gradually decreasing every year. The NPA of NIBL is least (minimum) that all of other banks at the end of 2059/060. The high degree of negative correlation of different commercial banks between NPA and ROA and NPA and ROE indicates towards the inverse relation between NPA and ROA and NPA and ROE. It means the level of NPA effect the return on assets and return on shareholder’s equity. Therefore, banks should reduce their level of NPA to increase the ROA and ROE.

He recommends that the banks should have to take enough collateral while lending loan, appropriate financial analysis, supervision, monitoring and control should be done. Lastly, those banks having high level of NPA should take immediate action towards recovering their bad loan as possible as soon. In case of default to repay the loan recover principle and interest amount.

Shama Bhattarai (2004) has stated in her research “Implementation of Directives Issued by Rastra Bank: A comparative study of Nepal SBI Bank Limited and Nepal Bangladesh Bank Limited” to analyze the various aspects of NRB directives such as capital adequacy and loan classification and loan provisioning. In her view, the loan classification helps to the banks to monitor the quality of their loan and advances and to take step towards the remedial action in the credit quality of their loan and advances.

She concludes that the new provision of the banks will have its provision amount increasing in coming years and subsequently profitability of the banks will also come down. However, the true picture of the quality of assets will be painted in the coming year.

She recommends the banks should be very careful while analyzing the paying capacity of its credit clients. With longer period of past due, the bank will end up increasing its provision which will keep the bottom line low if the bank is non careful (Bhattarai, 2004: 95).

2.2.3 Research Gap

From the above study it can be said that the NPA is one of the challenging problem of the commercial banks in Nepal, which is followed by increasing loan loss provisioning. It is found that some research in the related topic but no research was found in detailed research and analysis of non-performing assets of commercial banks. Related articles and thesis have already been reviewed which helps to this study.

The purpose of this research is to develop some expertise in one’s area, to see what new contribution can be made to receive some ideas, knowledge and suggestions in relation to latest information of NPA. The previous studies can’t be ignored because they provide the foundation to the present study. In other words, there has to be continuity in research. This continuity in research is ensured by linking the present study with the past research studies. Here, it is clear that the new research cannot be found on that exact topic, i.e. Non-performing assets of commercial banks: cause and effect. Therefore, to fulfill this gap, this research is selected. To complete this research work: many books, journals, articles and various published and unpublished dissertations are followed as guideline to make the research easier and smooth. In this regard, here this researcher going to analyze the non-performing assets of commercial bank, which is considered only on Nepal Bank Limited (NBL). Here the research problem is to analyze the impact of NPA on profitability. To achieve this main objective, various financial and statistical tools are used to draw conclusion and provide recommendation to concern authority.

CHAPTER - THREE

RESEARCH METHODOLOGY

3.1 Introduction

Research is undertaken not to solve the problem existing in the work setting but also to add or contribute to the general body of knowledge in a particular area of interest to the researcher. Research is thus a knowledge building process. It generates new knowledge, which can be used for different purpose it is used to build a theory, develop policies, supports decision making and solve problems. With the open of new frontiers of knowledge through research new concept and theories are developed to explain, verify and analyze the social phenomena (Wolf and Pant, 1999: 204).

Research Methodology is a way to systematically solve the research problem (Kothari, 1990:10). It may be understood as a science of studying how research is done scientifically. In it, we study the various steps that are generally adopted by a researcher, studying his research problem among with the logic behind them.

A research methodology helps us to find out accuracy, validity and suitability. The justification on the present study cannot be obtained without help of proper research methodology. For the purpose of achieving the objectives of study, the applied methodology will be used. The research methodology used in the present study is briefly mentioned below.

This topic presents the short outline of the methods applied in the process of analyzing the non-performing assets of the Nepal Bank Limited (NBL). Research is a systematic method of finding out the solution to a problem whereas research methodology refers to the various sequential steps to adopt by a researcher in studying a problem with certain objective ink view.

This chapter looks into the research design, nature and sources of data, data collection procedure and tools and techniques of analysis.

3.2 Research Design

A research design is the arrangement of condition for collection and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure. For the analysis of non-performing assets of Nepal Bank Limited, analytical as well as descriptive designs applied to achieve the objective of the research.

Thus, a research design is a plan for the collection and analysis of data. It presents a series of guideposts for the researcher to progress in the right direction in order to achieve the goal. The design may be a specific presentation of the various steps in the problems, formulation of hypothesis, conceptual clarity, methodology, survey of literature and documentation, bibliography, data collection, testing of the hypothesis, interpretation, presentation and report writing. Generally, a common research design possesses the five basic elements viz. (i) selection of problem (ii) methodology (iii) data gathering (iv) data analysis and (v) report writing.

The research design asks, what approach to the problem should be taken, what methods will be used, what strategies will be used, what strategies will be effective etc. Identification, selection and formulation of a research problem may be considered as planning stage of a research and the remaining activities refer to the design, operation and completion of the research study.

A research design is the specification of methods and procedures of acquiring the information needed. It is the overall operational pattern of framework, of the project that stipulates what information is to be collected from which sources and what procedure. If it is a good design, it will ensure that the information obtained is relevant to the research questions and that it was collected objective and economical procedures.

Review of literature means reviewing research studies or other relevant propositions in the related area of the study so that all the past studies, their conclusions and deficiencies may be known and further research can be conducted. It is an integral and mandatory process in research works.

The main reason for a full review of research in the past is to know the outcomes of those investigations in areas where similar concepts and methodologies had been used successfully. Further, an extensive or even extensive or even exhaustive process of such review may offer vital links with the various trends and phases in the researchers in one's area of specialization, familiarizing with the characteristic percepts, concepts and interpretation, with the special terminology, with the rationale for understanding one's proposed investigation.

In this connection a review of previous related research projects will help the researcher to formulate a satisfactory structure for the project.

There is significant importance of review of literature in any types of research works, some of which are:

1. Identification of research problem and relevant variables.
2. Avoidance of repetition.
3. Synthesis of prior works.
4. Determining meaning and relationship among variables.

3.3 Data Collection Techniques

The researcher used only secondary data collection techniques. Secondary data are collected from some reports, publications, official records etc. So the major sources of secondary data for this study are as follows:

a) Annual reports of the bank.
b) Published and unpublished bulletins, reports of the bank.
c) Published and unpublished bulletins, reports of the Nepal Stock Exchange.
d) Previous studies and reports.
e) Unpublished official records.
f) "Banking and Financial statistics" report of Nepal Rastra Bank Magazines.
g) Journals and other published and unpublished related documents and reports for Central Library of T.U. and Library of Nepal Rastra Bank.
h) Various Internet Websites.
i) Other published materials.

3.4 Methods of Data Analysis

Data, valuable information and other things collected from different sources in raw form and in the initial stage judging independently do not help for decision but proper arrangement of them is essential thus the collected information and facts have been properly processed, tabulated, for the purpose of analysis and analyzed using relevant financial and statistical tools to achieve the objective.

3.5 Tools used for analysis of Data

Mainly financial methods are applied for the purpose of this study. Appropriate statistical tools are also used. Correlation analysis regarded as major one for this research.

To make the study more specific and reliable, the researcher uses two types of tool for analysis:

i) Financial Tools
ii) Statistical Tools and
iii) Trend Analysis

3.5.1 Financial Tools:

For the sake of analysis, various financial tools were used. The basic tools used were ratio analysis. Besides it, income and expenditure analysis along with cash flow analysis have been used.

3.5.1.1 Ratio Analysis:

Ratio analysis is a powerful and the most widely used tool of financial analysis. A ratio defined as "The indicated quotient of two mathematical expressions" and as the relationship between two or more things (Webster's New Collection Dictionary, 1975: 958).

A ratio is a figure or a percentage representing the comparison of one-dollar amount with some other dollar amount as a base (Roy, 1974: 97). Ratio analysis is a widely used tool of financial analysis. It is defined as the systematic use of ratio to interpret the financial statements so that the strength and weakness of a firm as well as its historical performance and current financial condition can be determined. In financial analysis a ratio is used as an index or yardstick for evaluating the financial position and performance of a firm. Ratio helps to summarize the large quantities of financial data and to make qualitative judgment about the firm's financial performance (Pandey, 1979: 97).

A large number of ratios can be generated from the components of profit and loss account and balance sheet. They are sound reasons for selecting different kinds of ratios for different types of situations. For this study, ratios are categorized into the following major headings:

3.5.1.1.1 Liquidity Ratios:

Liquidity refers to the ability of a firm to meet its short-term or current obligations. So liquidity ratios are used to measure the ability of a firm to meet its short-term obligations and from them the present cash solvency as well ability to remain solvent in the event of adversities of the same can be examined (Van Horne, 1999: 693).

Inadequate liquidity can lead to unexpected cash short falls that must be covered at inordinate costs, thus reducing profitability. In the worst case, inadequate liquidity can lead to the liquidity insolvency of the institution. On the other hand, excessive liquidity can lead to low asset yields and contribute to poor earnings performance (Scott, 1992: 140).

To find out the ability of bank to meet their short-term obligations, which are likely to mature in the short period, these ratios are calculated. The following ratios are developed under the liquidity ratios to identify the liquidity position.

i. Current Ratio

Current ratio indicates the ability of the bank to meet its current obligation. It measures the relationship between current assets and current liabilities, which is expressed as:

$$\text{Current ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

Current assets are those assets which can be converted into cash within a year and so it includes cash and bank balance, investment in treasury bills, bills purchased and discounted, customer acceptances liabilities, prepaid expenses, bills for collection, likewise current liabilities denotes current account deposits, saving account deposits, margin deposits, bills payable, call deposits, bank overdraft, inter bank overdraft, inter bank reconciliation account, provisions, customer's acceptance liabilities etc.

ii. Liquid Fund to Current Liability Ratio

It indicates the ability of bank to discharge its liquidity risk. Liquid fund are those assets, which can be converted into cash with in a short period without any decline in their volume.

$$\text{Liquid fund to current liability ratio} = \frac{\text{Liquid Fund}}{\text{Current Liabilities}}$$

iii. Cash and Bank Balance to Total Deposit Ratio

Cash and bank balance are the most liquid current assets. This ratio measures the percentage of most liquid fund with the bank to make immediate payment to the depositors. Both higher and lower ratios are not desirable. The reason is that if bank maintains higher ratio of cash, it has to pay interest on deposits and some canings may be lost. In contrast, if a bank maintains low ratio of cash, may fail to make payment for the demands of the depositors. So, appropriate cash reserve should be maintained properly. This ratio shows the ability of banks immediate funds to cover their deposit. Higher the ratio shows higher liquidity position and ability to cover the deposits and vice versa. It can be calculated by dividing 'cash and bank balance' by deposits. This ratio can be calculated using the following formula.

$$\text{Cash and bank balance to total deposit ratio} = \frac{\text{Cash and Bank Balance}}{\text{Total Deposits}}$$

iv. Cash and Bank Balance to Current Deposit Ratio

Cash and bank balance are the most liquid current assets. This ratio measures the percentage of most liquid fund with the current assets. Higher ratio indicates the bank's sound ability to meet the daily cash requirement of their customer's deposit. If bank maintain low ratio, bank may not be able to make the payment against cheques. So bank has to maintain cash and bank balance to current ratio properly. This ratio is computed to disclose the soundness of the company to pay total calls made of current deposits. It can be expressed as:

$$\text{Cash and bank balance to current deposit ratio} = \frac{\text{Cash and Bank Balance}}{\text{Current Deposits}}$$

3.5.1.1.2 Activity/Efficiency Ratios:

It is also known as turnover or efficiency ratio or assets management ratio; measures how efficiently the firm employs the assets. Turnover means; how many times the assets flow through a firm's operations and into sales (Kulkarni, 1994: 138). Greater rate of turnover or conversion indicates more efficiency of a firm in managing and utilizing its assets, being other things equal. Various ratios are examined under this heading.

i. Loan and Advances to Total Deposit Ratio

Commercial banks utilize the outsider's fund for profit generation purpose. Loan and advances to total deposit ratio shows whether the banks are successful to utilize the outsiders funds (i.e. total deposits) for the profit generating purpose on the loan and advances or not. Generally, a high ratio reflects higher efficiency to utilize outsider's fund and vice-versa. The ratio can be calculated by using following formula.

$$\text{Loan and advances to total deposit ratio} = \frac{\text{Loan and Advances}}{\text{Total Deposits}}$$

ii. Loan and Advances to Total Assets Ratio

It measures the ability in mobilizing total assets into loan and advances for profit generating income. A higher ratio is considered as an adequate symbol for effective utilization of total assets of bank into loan and advances which creates opportunity to earn more and more. It is calculated as:

$$\text{Loan and advances to total assets ratio} = \frac{\text{Loan and Advances}}{\text{Total Assets}}$$

iii. Total Assets to Total Liability Ratio

The total assets of the bank should play active role in profit generating through lending activities. This ratio measures the bank's ability to multiple its liability into assets. It is always recommended to have higher ratio of total assets to total liabilities ratio since it signifies overall increases of credit. The higher ratio indicates the higher productivity.

$$\text{Total assets to total liability ratio} = \frac{\text{Total Assets}}{\text{Total Liability}}$$

iv. Total Investment to Total Deposit Ratio

A commercial bank may mobilize its deposit by investing its fund in different securities issued by government and other financial and non-financial companies. Effort has been made to measure the extent to which the banks are successful in mobilizing the total deposit on investment. A high ratio is the indicator of high success to mobilize the banking fund as investment and vice-versa.

$$\text{Total investment to total deposit ratio} = \frac{\text{Total Investment}}{\text{Total Deposit}}$$

3.5.1.1.3 Profitability Ratios:

Profit is the difference between revenues and expenses over a period of time. A company should earn profit to survive and to grow over a long period of time. So profits are essential, but profit earning is not the ultimate aim of company and it should never be earned at the cost of employees, customer and society.

Profitability ratios are the indicators of degree of managerial success in achieving firm's overall goals (pradhan, 1996: 41). It shows the overall efficiency of the business concern. The following ratios are calculated under the profitability ratios:

i. Return on Loan and Advances Ratio

This ratio measures the earning capacity of the commercial banks through its fund mobilization as loan advances. Higher ratio indicates greater success to mobilize fund as loan and advances and vice versa. Mostly loan and advances include cash credit, overdraft, bills purchased and discounted.

$$\text{Return on loan and advances} = \frac{\text{Net Profit}}{\text{Loan \& Advances}}$$

ii. Net Profit/Loss to Total Assets Ratio

The ratio is useful to measure how well management uses all the assets in the business to generate an operating surplus. Higher the ratio indicates the higher efficiency in the utilization of total assets and vice-versa. The ratio is low due to low profit. In other words, it is low utilization of bank assets and over use of higher interest bearing amount of debt and vice-versa. In this study, net profit/loss to total assets ratio is examined to measure the profitability of all the financial resources in bank-assets and is calculated by applying the following formula:

$$\text{Net profit/loss to total assets ratio} = \frac{\text{Net Profit/Loss}}{\text{Total Assets}}$$

iii. Interest Income to Total Loan and Advances Ratio

It tells income as interest from total loan and advances. It is useful to know the fact that whether the loan has given good return or not. We can increase interest income by taking good issuing and recovery credit policy. High return shows the soundness of credit policy. It is calculated by using the following formula:

$$\text{Interest income to total loan and advances ratio} = \frac{\text{Interest Income}}{\text{Total credit \& Advances}}$$

iv. Earning Per Share (EPS)

EPS is one of the most widely quoted statistics when there is a discussion of a company's performance or share value. It is the profit after tax figure that is divided by the number of common shares to calculate the value of earnings per share. This figure tells us what profit the common shareholders for every share held have earned. A company can decide whether to increase or reduce the number of shares on issue.

This decision will automatically affect the earnings per share. The profits available to the ordinary shareholders are represented by net profit after taxes and preference dividend. Symbolic expression of EPS is given below.

$$\text{EPS} = \frac{\text{Net Profit after taxes}}{\text{Number of common stocks outstanding}}$$

3.5.1.1.4 Lending Efficiency Ratio:

The efficiency of a firm depends to a large extent on the efficiency with which its assets are managed and utilized. This ratio is concerned with measuring the efficiency of bank. This ratio also shows the utility of available fund. The following are the various type of lending efficiency ratios:

i. Loan Loss Provision to Total Loan and Advances Ratio

Loan loss provision to total loan and advances describes the quality assets that a bank holds. The provision for loan loss reflects the increasing probability of non-performing loan. The provision of loan mean the net profit of the banks will come down by such amount. Increase in loan loss provisions decrease in profit result to decrease in dividends but it's positive impact is that strengthens financial conditions of the bank by controlling the credit risk and reduced the risks related deposits. So it can said that loan suffer for short term while the full financial conditions and safety of loans will make bank's prosperity resulting increasing profits for long term. The low ratio indicates the good quality of assets in total volume of loan and advances. High ratio indicates more risky assets in total volume of loan and advances.

$$\text{Loan loss provision to total loan and advances} = \frac{\text{Loan Loss Provision}}{\text{Total Loan and Advances}}$$

ii. Non-Performing Loans to Total Loan and Advances Ratio

NRB has directed all the commercial banks to create loan loss provision against the doubtful and bad debts. But both of our concerned banks have not provided data on non-performing loan in balance sheet and profit and loss account.

$$\text{Non-performing loan to total loan and advances} = \frac{\text{Non – Performing Loan}}{\text{Total Loan \& Advances}}$$

3.5.1.2 Limitations of Ratio Analysis:

Ratio analysis is suffered from some inherent limitations that are directly inherited from financial statements. Some of the most common weaknesses of ratio analysis are as follows:

i. The firms or industry although apparently comparable in respect to size, age, location; product mix and technology may not be really comparable if they are following different accounting methods.

ii. Financial statement records past transactions. They are, thus an index of what happened in the past. They do not show the current position of the business. Evidently ratio analysis is also primarily concerned with analyzing the past, which may or may not be relevant today. It is thus a sort of 'Post-Mortem' analysis rather than a guide for decision-making.

iii. In the context of persistent price level changes, intra firm trends analysis losses much of its operational significance.

iv. The differences in the definitions of items in the balance sheet and the income statement make the interpretation of ratios difficult.

v. Some times ratio analysis may suffer from what is known as fallacy of misplaced concreteness (Singh, 1993: 101).

Although, various limitations of ratio analysis and doubt may arise about the valid measure of the financial performance but they are used widely to measure the financial performance of the firm.

3.5.2 Statistical Tools:

For supporting the study, statistical tool such as Mean, Standard Deviation, Coefficient of Variation, Correlation, Trend Analysis, Hypothesis and diagrammatic cum pictorial tools have been used under it.

3.5.2.1 Arithmetic Mean (X):

Averages are statistical constants, which enable us to comprehend in a single effort of the whole (Gupta, 2000: 357). It represents the entire data by a single value. It provides the gist and gives the bird's eye view of the huge mass of unwieldy numerical data. It is calculated as:

$$\bar{x} \quad = \quad \frac{x}{N}$$

Where,

$\bar{x}$ = Arithmetic mean

N = Number of observations

$\sum x$ = Sum of observations

3.5.2.2 Standard Deviation (S.D.)

The standard deviation is the square root of mean squared deviations from the arithmetic mean and is denoted by S.D. or * (Shrestha, 1991: 43). It is used as absolute measure of dispersion or variability. It is calculated as:

$$\pm\ X \quad \sqrt{\frac{X^{2}}{N}\ Z\ \frac{X}{N}^{2}}$$

Where,

± X Standard deviation

$\frac{\sum X^2}{N}$ = Sum of squares of observations divided by number of observation

$\frac{\sum X}{N}$ = Sum of observation divided by number of observation

3.5.2.3 Coefficient of Variation (C.V.)

The Co-efficient of variation (C.V.) is the relative measure based on the standard deviation and is defined as the ratio of the standard deviation to the mean expressed in percentage (Shrestha, 1991: 45). It is independent of units. Hence, it is a suitable measure for comparing variability of two series with same or different units. A series with smaller C.V. is said to be less variable or more consistent or more homogeneous or more uniform or more stable than the others and vice versa. It is calculated as:

$$C.V. = \frac{\sigma}{\bar{x}} \times 100\%$$

Where

C.V.= Coefficient of Variation

σ = Standard deviation

$\bar{x}$ = Arithmetic mean

3.5.2.4 Correlation Coefficient (r):

Correlation may be defined as the degree of linear relationship existing between two or more variables. These variables are said to be correlated when the change in the value of one results change in another variable. Correlation is of three types. They are Simple, Partial and Multiple correlations. Correlation may be positive, negative or zero. Correlation can be classified as linear or non-linear. Here, we study simple correlation only. In simple correlation the effect of others is not included rather these are taken as constant considering them to have no serious effect on the dependent variable (Shrestha, 2051: 31). It is calculated as:

$$rx_1x_2 = N\sum x_1x_2 - (\sum x_1)(\sum x_2)$$

Where,

rx_1x_2 = Correlation between x_1 and x_2

3.5.2.5 Probable Error:

The probable error of the coefficient of correlation helps in interpreting its value. With the help of probable error, it is possible to determine the reliability of the value of the coefficient in so far as it depends on the conditions of random sampling. The probable error of the coefficient of correlation is obtained as follows:

$$P.E. = 0.6745 \frac{1-r^2}{\sqrt{N}}$$

Where,

r= Correlation Coefficient

N=Number of pairs of observations

If the value of ‘r’ is less than the probable error, there is no evidence of correlation, i.e., the value of ‘r’ is not at all significant. Then, if the value of ‘r’ is more than six times of the probable error, the coefficient of correlation is practically certain, i.e., the value of ‘r’ is significant.

3.5.3 Trend Analysis:

The tools that are used to show grandly increase and decrease of variable in a period of time is known as trend analysis. With the help of trend analysis; the tendency of variables over the period can be seen clearly. Here, trend analysis of deposit, investment and profit has been conducted.

CHAPTER - FOUR

PRESENTATION AND INTERPRETATION OF DATA

4.1 Introduction

Under this part, the collected data through secondary sources have been represented in the suitable formats (i.e. tables and charts), analyzed using various statistical and financial tools, and certain inferences and interpretation have also been made finally.

4.2 Ratio Analysis

Ratio analysis is a widely used tool of financial analysis. It is defined as the systematic use of ratio to interpret the financial statements so that the strength and weakness of a firm as well as i4s historical performance and current financial condition can be determined. For this study, the following ratios are calculated:

4.2.1 Loan and Advances to Total Deposit Ratio

Loan and advances to total Deposit ratio shows whether the banks are successful to utilize the outsiders funds (i.e. total deposits) for the profit generating purpose or not. Generally, a high ratio reflects higher efficiency to utilize outsider's fund and vice-versa. The ratio can be calculated by using following formula:

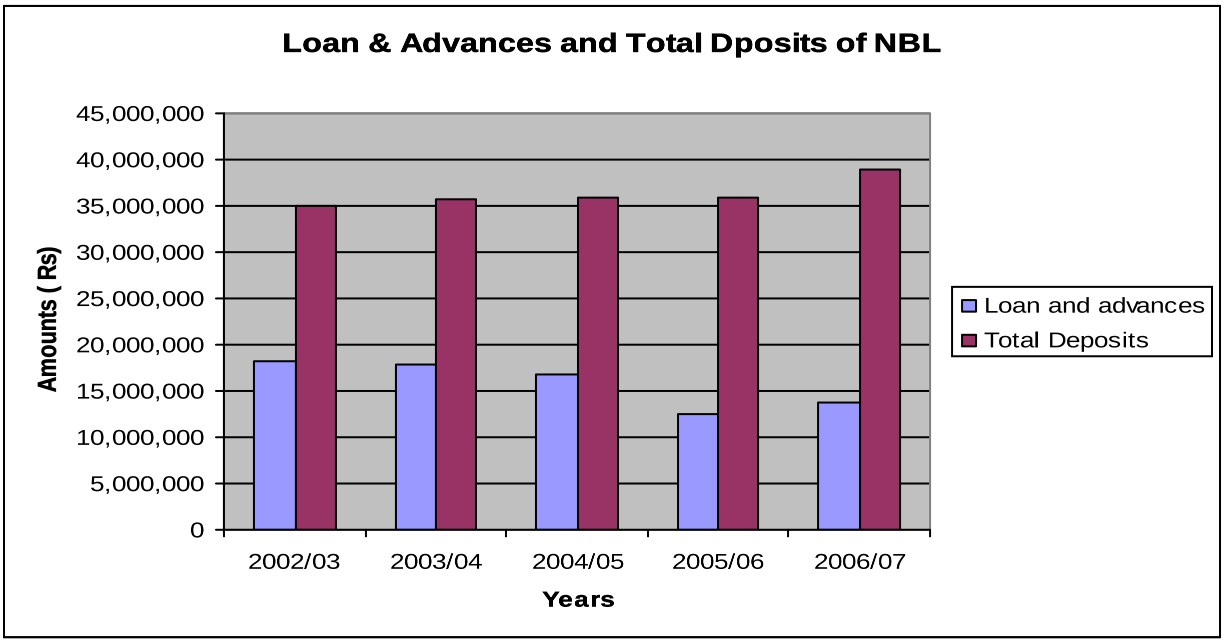
$$\text{Loan and advances to total deposit ratio} = \frac{\text{Total loan \& Advances}}{\text{Total Deposits}}$$

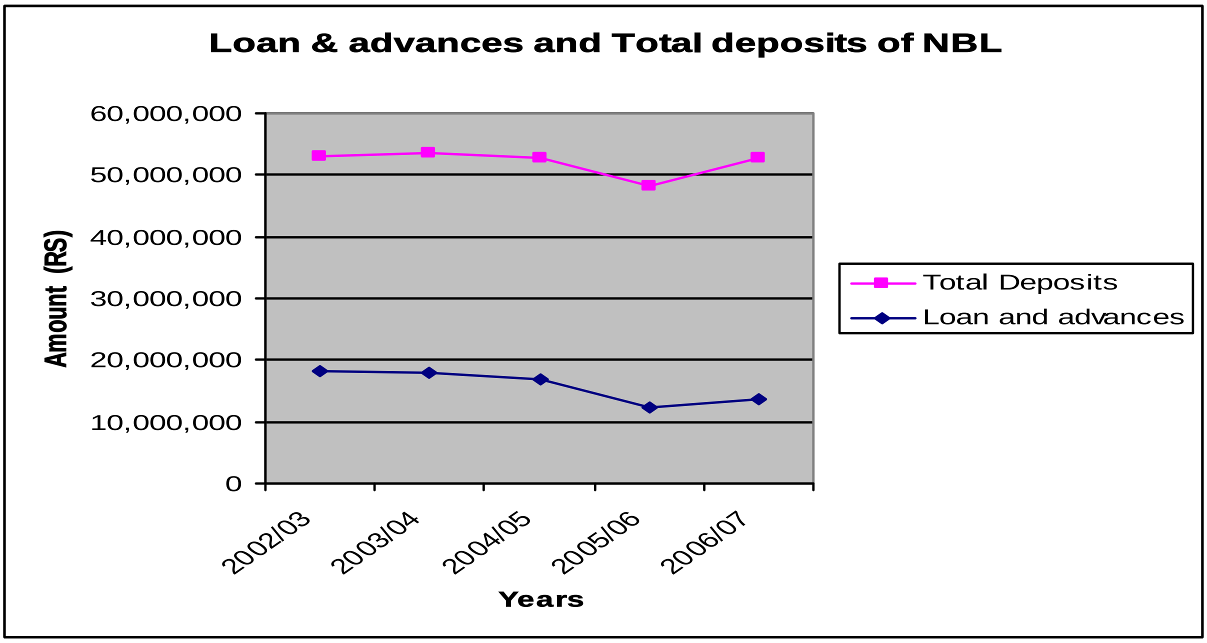
Table: 4.1

Loan & Advances to Total Deposit Ratio of NBL

Rs. in 000

Year	Loan and advances	Total Deposits	Ratio (%)
2002/03	18,132,327	35,014,001	51.79
2003/04	17,937,658	35,735,044	50.20
2004/05	16,866,546	35,934,164	46.94
2005/06	12,441,554	35,829,765	34.72
2006/07	13,756,620	39,014,204	35.26
Average	**15,826,941**	**36,305,436**	**43.59**





The above table shows the actual figure of loan & advance, total deposits, there averages and loan & advance to total deposit ratio of latest five fiscal years of Nepal Bank Limited. The average loan and advance is Rs. **15,826,941** thousand and average Deposit is Rs. **36,305,436**. In the fiscal year 2002/03 loan & advance to total deposit ratio is highest i.e. 51.79% but is in decreasing trend in the following years. The average loan & advance to total deposit ratio is 43.59% over the study period.

4.2.2 Non- performing Asset to Total Loan and Advance Ratio

Non-performing assets to total loan & advances ratio shows the actual figure of NPA over the total lending of bank. It is the base ratio to measure efficiency of lending department. Here, lower ratio reflects higher efficiency to provide good lending and vice versa. The ratio is calculated by using following formula:

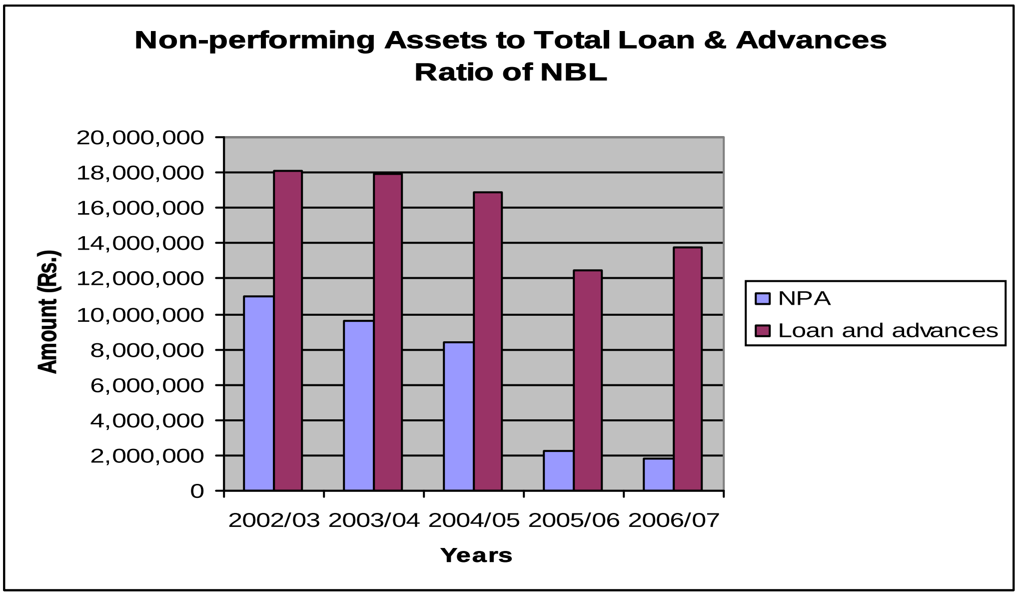
$$\text{NPA to total loan \& advances ratio} = \frac{\text{Non-performing Assets}}{\text{Total Loan \& Advances}}$$

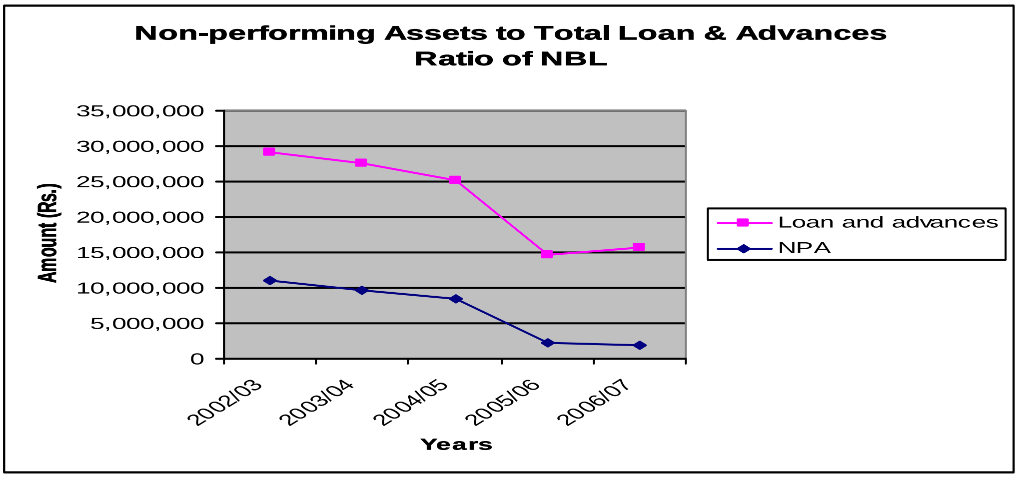
Table: 4.2

Non-performing Assets to Total Loan & Advances Ratio of NBL

Rs. in 000

Year	NPA	Loan & advances	Ratio (%)
2002/03	10,964,913	18,132,327	60.47
2003/04	9,640,082	17,937,658	53.74
2004/05	8,372,108	16,866,546	49.64
2005/06	2,262,183	12,441,554	18.18
2006/07	1,856,049	13,756,620	13.49
Average	**6,619,067**	**15,826,941**	**39.11**





The above table reflects the actual figures of non-performing assets, Total Loan and advances & their ratios of NBL for the latest five fiscal years period. The average NPA for the period is Rs.6, 619,067 and average Loan and advance is Rs.15, 826,941. The ratios in the years 2002/03, 2003/04, 2004/05, 2005/06 & 2006/07 are 60.47, 53.74, 49.64, 18.18 &13.49% respectively. The highest ratio is 60.47% in the year 2002/03 and it is in decreasing continuously in the following years and the average ratio is 39.11% for the period.

4.2.3 Non- performing Asset to Total Assets Ratio

Non-performing assets to total assets ratio shows the total default loan out of total assets. It measures the strength and weakness of bank in relation to financial condition. Normally, lower ratio reflects more efficiency in granting loan & advances and vice versa. The ratio is calculated as following formula:

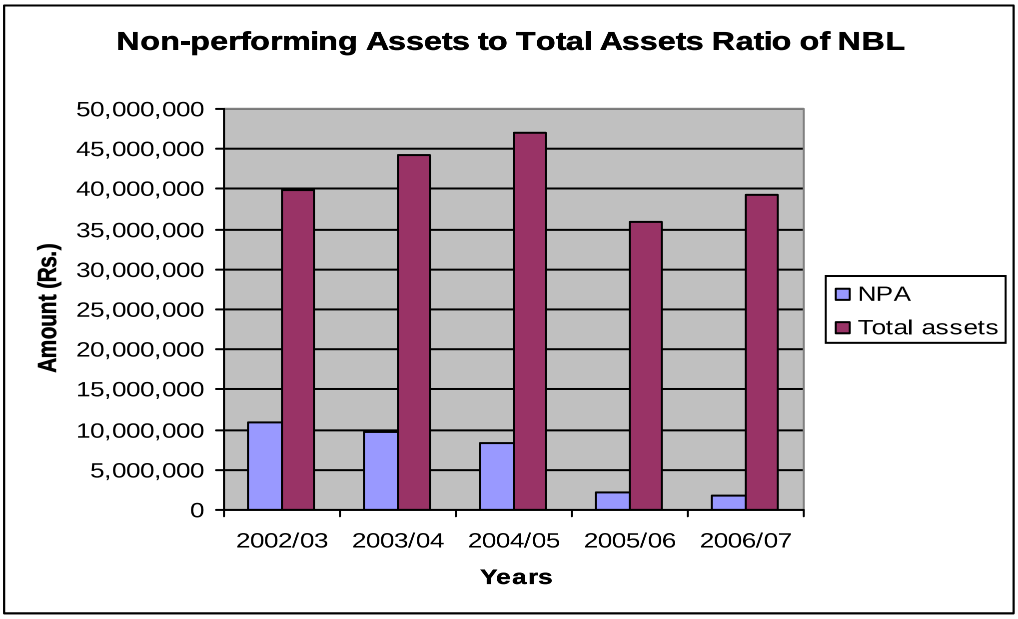
$$\text{NPA to total assets ratio} = \frac{\text{Non-performing Assets}}{\text{Total Assets}}$$

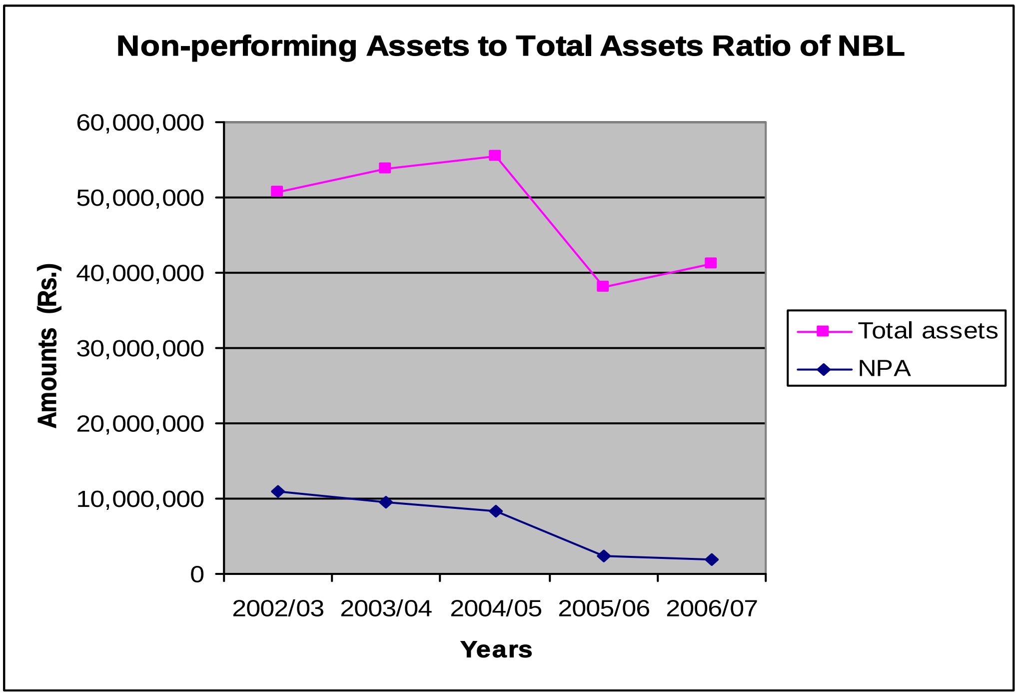
Table: 4.3

Non-performing Assets to Total Assets Ratio of NBL

Rs. in 000

Year	NPA	Total assets	Ratio (%)
2002/03	10,964,913	39,816,491	27.54
2003/04	9,640,082	44,161,880	21.83
2004/05	8,372,108	47,045,154	17.80
2005/06	2,262,183	35,918,905	6.30
2006/07	1,856,049	39,258,794	4.73
Average	**6,619,067**	**206,201,224**	**15.64**





The above table shows the actual figures of non-performing assets, total assets & their ratios of NBL over the latest five fiscal years. The average NPA is Rs.6,619,067 and the average total assets is Rs.206,201,224.The ratio 27.54% which is highest is in the year 2002/03 & 4.73% which is lowest is in 2006/07. The average NPA to Total Assets ratio is 15.64% for the study period.

4.2.4 Loan Loss Provision to Non- performing Asset Ratio

Loan loss provision to non-performing assets ratio shows the provision made for future loss so that the bank can remove from worst condition and could operate it as smoothly. Higher ratio reflects the effective in relation to future loss but it directly affected in profitability and vice versa. The ratio is calculated by using following formula:

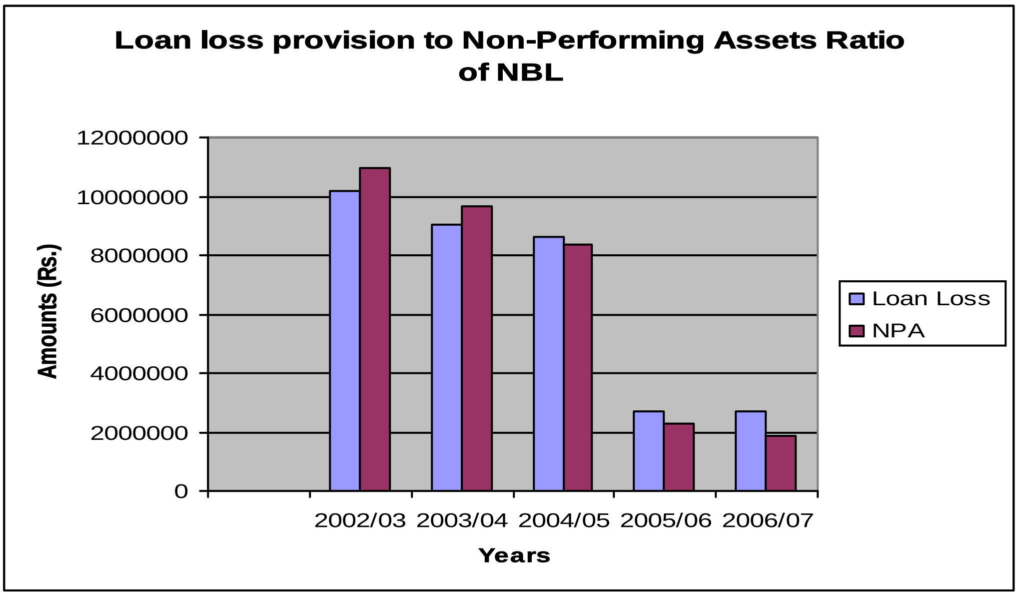
$$\text{Loan loss Provision to NPA ratio} = \frac{\text{Loan Loss Provision}}{\text{Non-performing Assets}}$$

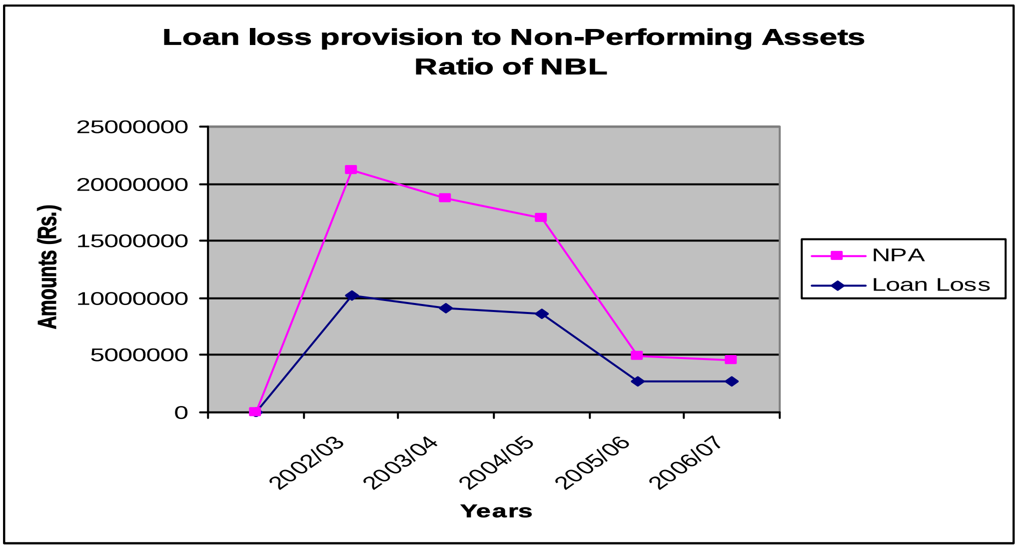
Table: 4.4

Loan Loss Provision to Non-performing Assets Ratio of NBL

Rs. in 000

Year	Loan Loss Provision	NPA	Ratio (%)
2002/03	10,161,229	10,964,913	92.67
2003/04	9,055,835	9,640,082	93.94
2004/05	8,647,636	8,372,108	103.29
2005/06	2,685,391	2,262,183	118.71
2006/07	2,698,142	1,856,049	145.37
Average	**6,649,647**	**6,619,067**	**110.80**





The above table shows the Loan loss Provision, non-performing assets & their ratios of NBL for the study period. The average Loan Loss provision for the period is Rs.6649647 and average NPA is Rs.6619067. The ratio in fiscal year 2006/07 is highest and i.e 145.37% and ratio in fiscal year 2002/03 is lowest i.e.92.67. The ratio is in increasing trend for the period.

4.2.5 Return to Total Assets Ratio

This ratio measures the profitability with respect to total assets. This ratio is examined to measure the profitability of all financial resources invested in the banks assets. The ratio is calculated by using following formula:

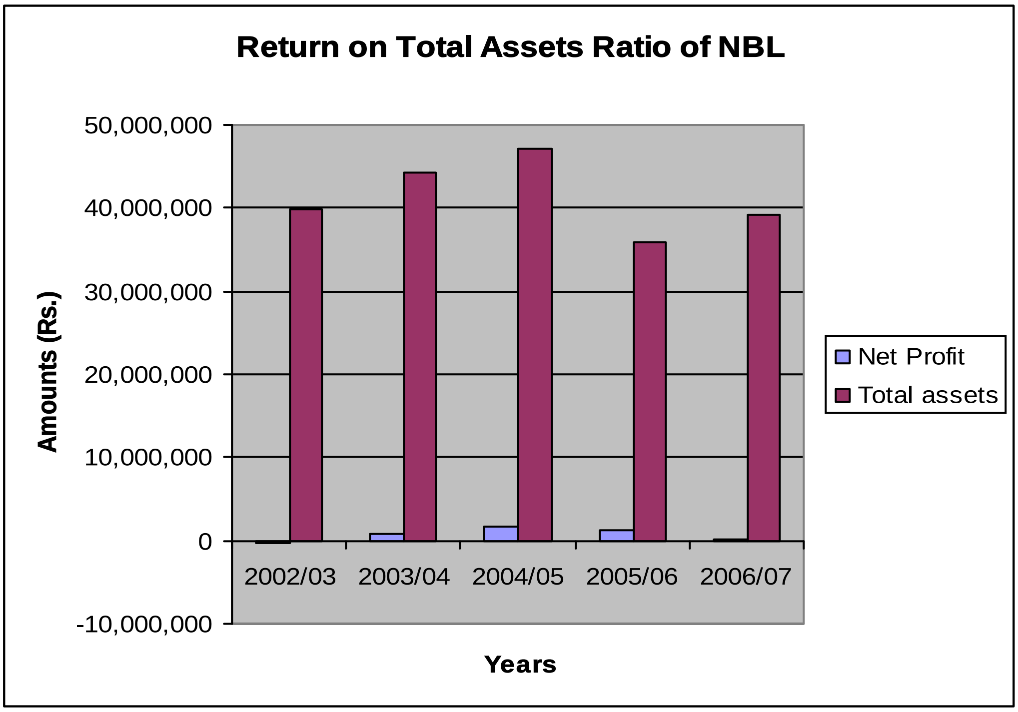
$$\text{Return on total assets} = \frac{\text{Net Profit}}{\text{Total Assets}}$$

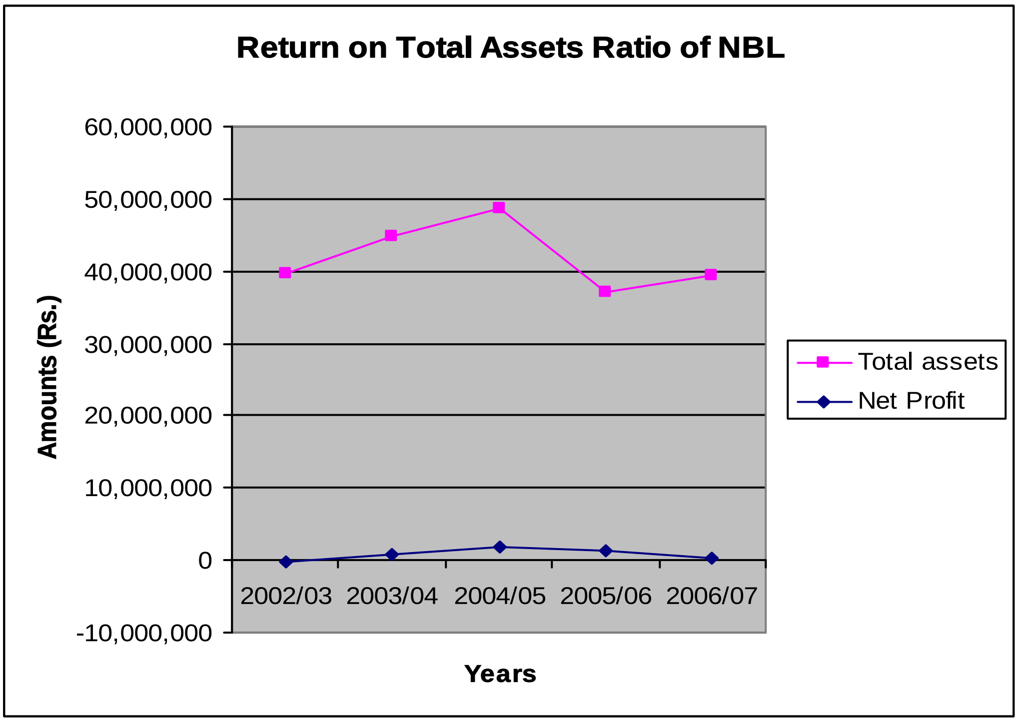
Table: 4.5

Return on Total Assets Ratio of NBL

Rs. in 000

Year	Net Profit	Total assets	Ratio (%)
2002/03	-251,731	39,816,491	(0.632)
2003/04	710,391	44,161,880	1.609
2004/05	1,730,130	47,045,154	3.678
2005/06	1,207,265	35,918,905	3.361
2006/07	226,953	39,258,794	0.578
Average	**724,602**	**206,201,224**	**1.757**





The above table shows net profit, total assets and their ratios of NBL from the fiscal year 2002/03 to 2006/07.The average net profit for the period is Rs.724602 and average total assets is 206201224. In the study period the highest ratio is 3.678% in the fiscal year 2004/05 and the lowest ratio is (0.632%) in the fiscal year 2002/03. In an average the ratio remains at 1.757%.

4.2.6 Return on Shareholder's Equity Ratio

A return on shareholder's equity is calculated to see the profitability of owner's investment. The shareholder's equity includes paid-up share capital, share premium and reserves & surplus less accumulated losses. The return on shareholder's equity is net profit after taxes divided by shareholder's equity.

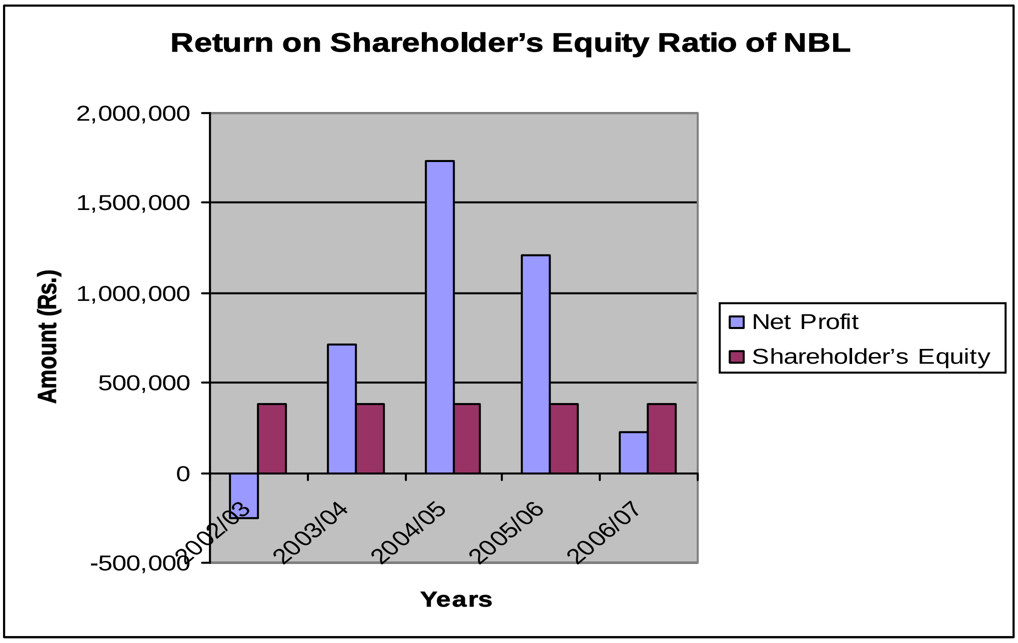
$$\text{Return on shareholder's equity} = \frac{\text{Net Profit after Tax}}{\text{Total Shareholder's Equity}}$$

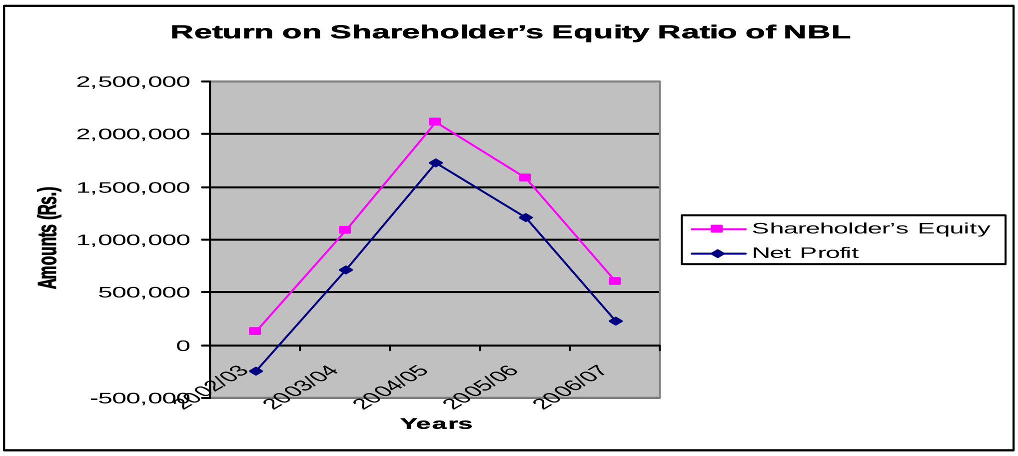
Table: 4.6

Return on Shareholder's Equity Ratio of NBL

Rs. in 000

Year	Net Profit	Shareholder's Equity	Ratio (%)
2002/03	-251,731	380,383	-66.18
2003/04	710,391	380,383	186.76
2004/05	1,730,130	380,383	454.84
2005/06	1,207,265	380,383	317.38
2006/07	226,953	380,383	59.66
Average	**7,24,602**	**380,383**	**190.49**





The above table shows the net profit, shareholder's equity and their relation of NBL from the fiscal year 2002/03 4o 2006/07.On this period, the average return is Rs.3,623,008. and the average shareholder's equity is Rs.380,383. The return on shareholder's equity is highest i.e. 454.84% in the fiscal year 2004/05 and the lowest i.e. 66.18% in fiscal year 2002/03. In an average the ratio remains at Rs.190.49 for the study period.

4.2.7 Non- performing Asset to Net Profit Ratio

Non-performing assets to net profit ratio shows the impact of NPA over the profitability of bank. There is inverse relationship between NPA and profit. If NPA increased, profit is decreased and if NPA decreased, profit is increased. Here, lower ratio reflects more efficiency to utilize outsides as well as insides fund in good lending and vice versa. The ratio is calculated by using & following formula:

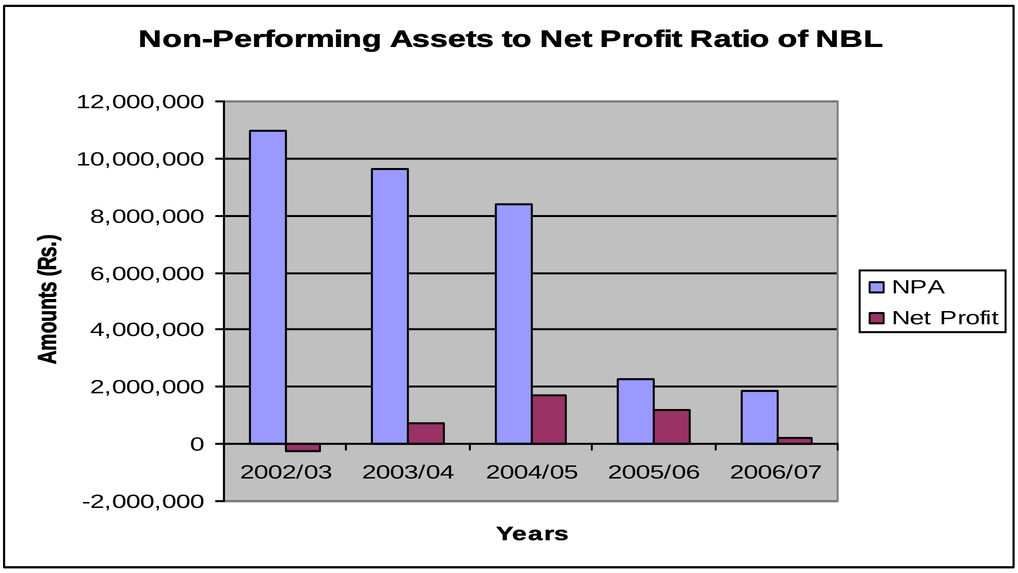
$$\text{NPA to net profit ratio} = \frac{\text{Non-performing Asset}}{\text{Net Profit}}$$

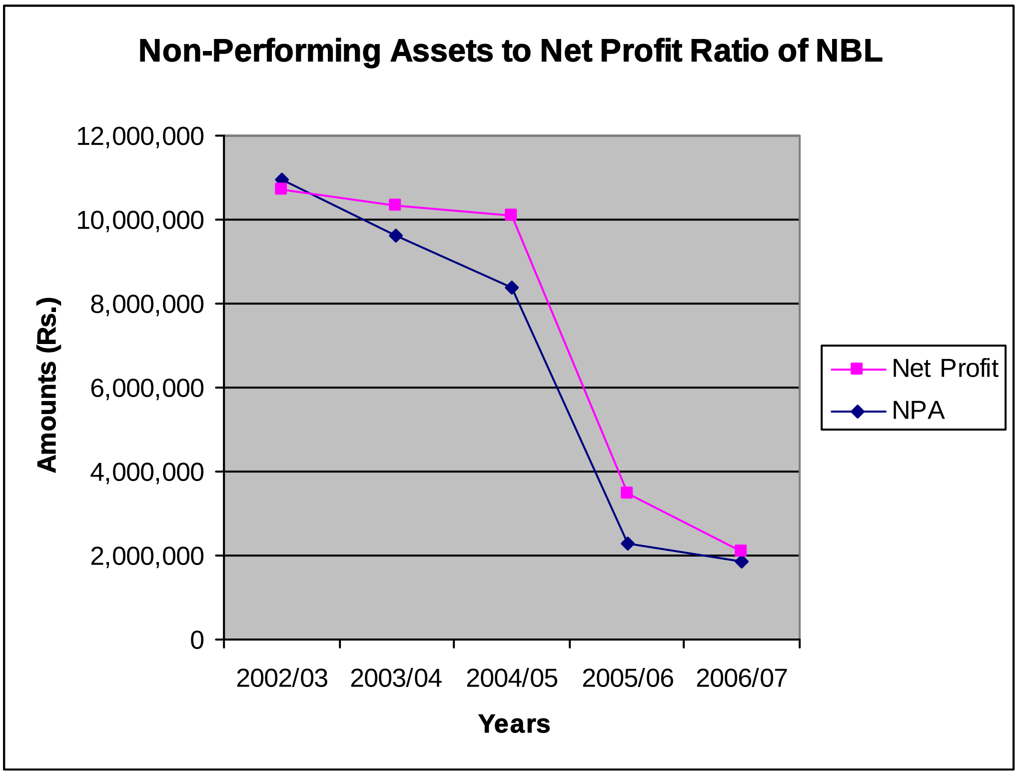
Table: 4.7

Non-performing Assets to Net Profit Ratio of NBL

Rs. in 000

Year	**NPA**	**Net Profit**	**Ratio (times)**
2002/03	10,964,913	-251,731	-4355.81
2003/04	9,640,082	710,391	1357.01
2004/05	8,372,108	1,730,130	483.90
2005/06	2,262,183	1,207,265	187.38
2006/07	1,856,049	226,953	817.81
Average	**6,619,067**	**724,602**	**913.48**





The above table shows the non-performing assets (NPA) to net profit ratio of NBL from the fiscal year 2002/03 to 2006/07.On this period, the highest ratio is 1357.01 times in the fiscal year 2003/04 and the lowest ratio is -4356.81 times in the fiscal year 2002/03. In an average the ratio remains at 913.48 times for the study period.

4.3 Correlation Analysis

Correlation may be defined as the degree of linear relationship existing between two or more variables. These variables are said to be correlated when the change in the value of one results change in another variable. It is calculated as:

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

Here,

N = Number of pairs of X and Y observed.

X = Values of loan and advances.

Y = Values of non-performing assets.

r = Pearson Ian correlation coefficient.

Here, the researcher calculated correlation coefficient of loan & advances and non-performing assets to show the relationship of these variables, which helps to identify the trend of NPA and loan & advances.

Table: 4.8

Computation of correlation coefficient between total loan & advances (X) and non-performing assets (Y) of NBL

year	Loan & Advances (x)	NPA (Y)	X	Y	X^2	Y^2	XY
2002/03	18,132,327	10,964,913	18.13	10.96	328.70	120.12	198.70
2003/04	17,937,658	9,640,082	17.94	9.64	321.84	92.93	172.94
2004/05	16,866,546	8,372,108	16.87	8.37	284.60	70.06	141.20
2005/06	12,441,554	2,262,183	12.44	2.26	154.75	5.11	28.11
2006/07	13,756,620	1,856,049	13.76	1.86	189.34	3.46	25.59
N=5	79134705	33095335	79.14	33.09	1279.23	291.68	566.54

Here, $N=5$, $\sum x=79134705$, $\sum y=33095335$, $\sum X=X/1000000=79.14$,

$\sum Y= y/1000000=33.09$, $\sum \mathbf{X^2}=1279.23$, $\sum \mathbf{Y^2} = 291.68$, $\sum \mathbf{XY}=566.54$

Now, coefficient of correlation (r) = $\dfrac{N\sum XY-\sum X\sum Y}{\sqrt{[N\sum X^2-(\sum X)^2]}\times\sqrt{[N\sum Y^2-(\sum Y)^2]}}$

$$= \frac{5\times566.54-79.14\times33.09}{\sqrt{[5\times1279.23-(79.14)^2]}\times\sqrt{[5\times291.68-(33.09)^2]}}$$

$$r = 0.97$$

According to above calculation, Karl Parson's coefficient of correlation between nonperforming assets and total loan and advances of NBL (r) is 0.97 . That means there is positive relationship between non performing assets ant total loan and advances of NBL . It denotes that if one variable out of them is increased that absolutely increased another variable in relation to 97%. But to find out the significant of insignificant relationship, here the researcher calculated probable error as following:

$$P.E.= 0.6745 \frac{1-r^2}{\sqrt{N}}$$

P.E. = 0.018

6 times P.E. = 0.1084

4.4 Trend Analysis

Trend analysis is the tools that are used to show grandly increase and decrease of variable in a period of time, is known as trend analysis. With the help of trend analysis; the tendency of variables over the period can be seen clearly. Here, trend analysis of deposits, loan & advances, non-performing assets and loan loss provision has been conducted.

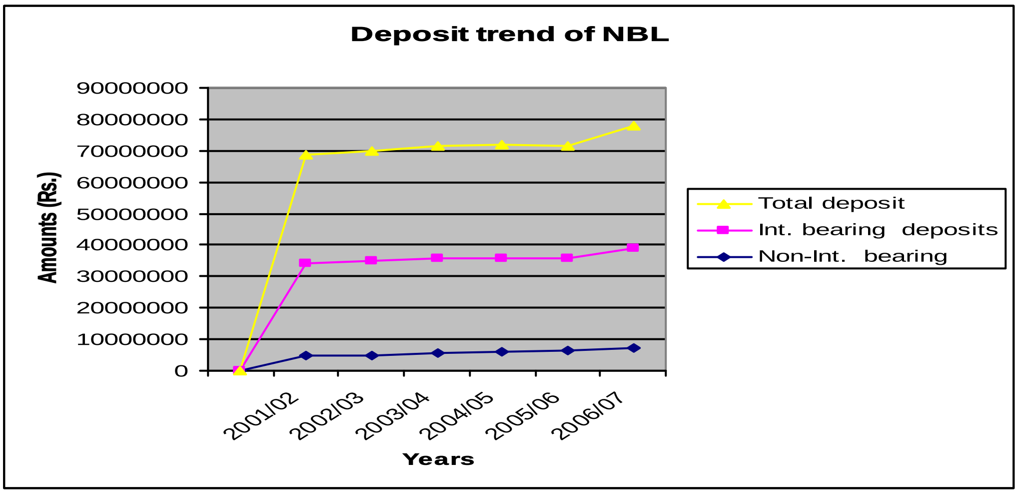
Deposit Trend

Table: 4.9

Deposit trend of NBL

Rs. in 000

Year	Non-Int. bearing deposits	Increase/ (decrease)	Int. bearing deposits	Increase/ (decrease)	Total deposit	Increase/ (decrease)
2001/02	4,678,450		29,586,396		34,264,846	
2002/03	4,996,006	6.788	30,017,995	1.459	35,014,001	2.19
2003/04	5,714,693	14.385	30,020,351	0.008	35,735,044	2.06
2004/05	6,135,632	7.366	29,798,532	-0.739	35,934,164	0.56
2005/06	6,479,234	5.600	29,350,531	-1.503	35,829,765	-0.29
2006/07	7,193,560	11.025	31,820,644	8.416	39,014,204	8.89
Average		9.033		1.528		2.68



The above table shows the deposit growth trend of NBL from the fiscal year 2002/03 to 2006/07. The highest growth is 14.385% in the fiscal Year 2003.04 in the comparison of fiscal year 2002/03 in Non-interest bearing deposit and 8.416% and 8.89% in fiscal year 2006/07 in comparison of fiscal year 2005/06 in Interest bearing deposit and total deposit respectively. The deposit growth is in negative i.e.-0.29 in the fiscal year 2005/06. The average growth rate is 2.68% for the period.

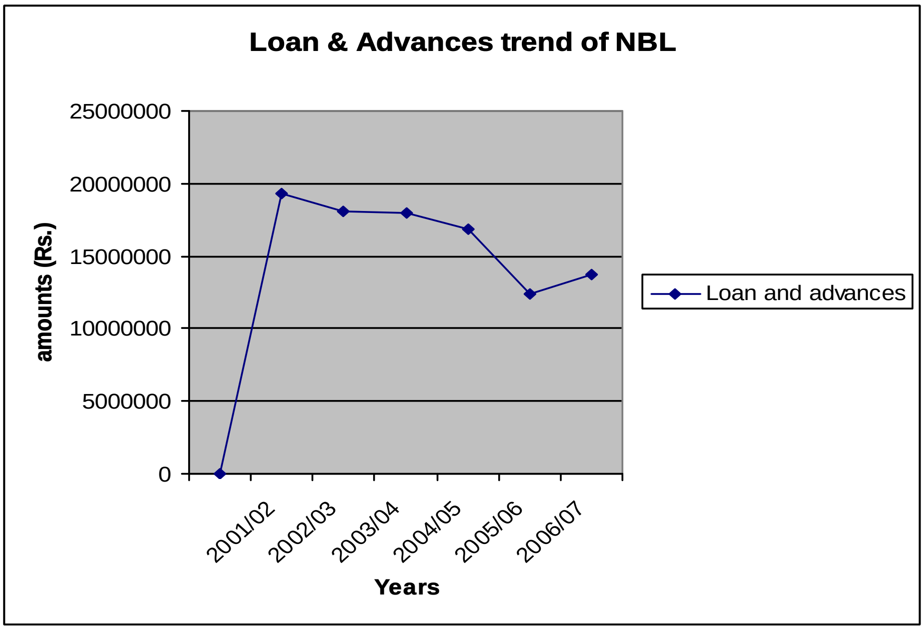
Loan & Advances Trend

Table: 4.10

Loan & Advances trend of NBL

Rs. in 000

Year	Loan and advances	Increase/(decrease)
2001/02	19,252,874	
2002/03	18,132,327	-5.82
2003/04	17,937,658	-1.07
2004/05	16,866,546	-5.97
2005/06	12,441,554	-26.24
2006/07	13,756,620	10.57
Average	**79,134,705**	**-5.71**



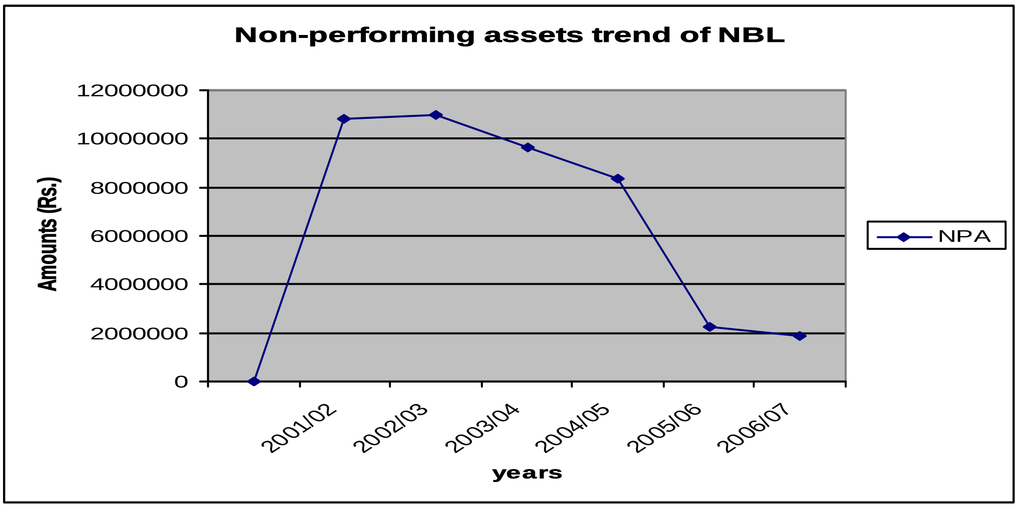
The above table depicted the loan & advances trend of NBL from the fiscal year 2002/03 to 2006/07. In first four fiscal year the case the loan & advances value is decreased and it has been increased in the last fiscal year of the study period. In fiscal year 2005/06, 26.24% loan and advance is decreased in the comparison of fiscal year 2004/05 which is the highest decrease over the study period and 10.57% increased in fiscal year 2006/07 in comparison of fiscal year 2005/07. The average decrease trend is 5.71% in the comparison of the subsequent year.

Non-performing Assets Trend

Table: 4.11
Non-performing assets trend of NBL

Rs. in 000

Year	NPA	Increase/(decrease)
2001/02	10,834,411	
2002/03	10,964,913	1.20
2003/04	9,640,082	-12.08
2004/05	8,372,108	-13.15
2005/06	2,262,183	-72.98
2006/07	1,856,049	-17.95
Average	**6,619,067**	**-22.99**



The above table shows the non performing assets trend of NBL from the fiscal year 2002/03 to 2006/07. In first fiscal year the NPA is increased and it has been decreased in the following four fiscal year of the study period. In fiscal year 2005/06, 72.98% NPA is decreased in the comparison of fiscal year 2004/05 which is the highest decrease over the study period and in fiscal year 2006/07, it is increased 1.20% in comparison of fiscal year 2005/07. The average NPA over the five fiscal year is Rs.**6,619,067** thousand and average decrease is 22.99%.

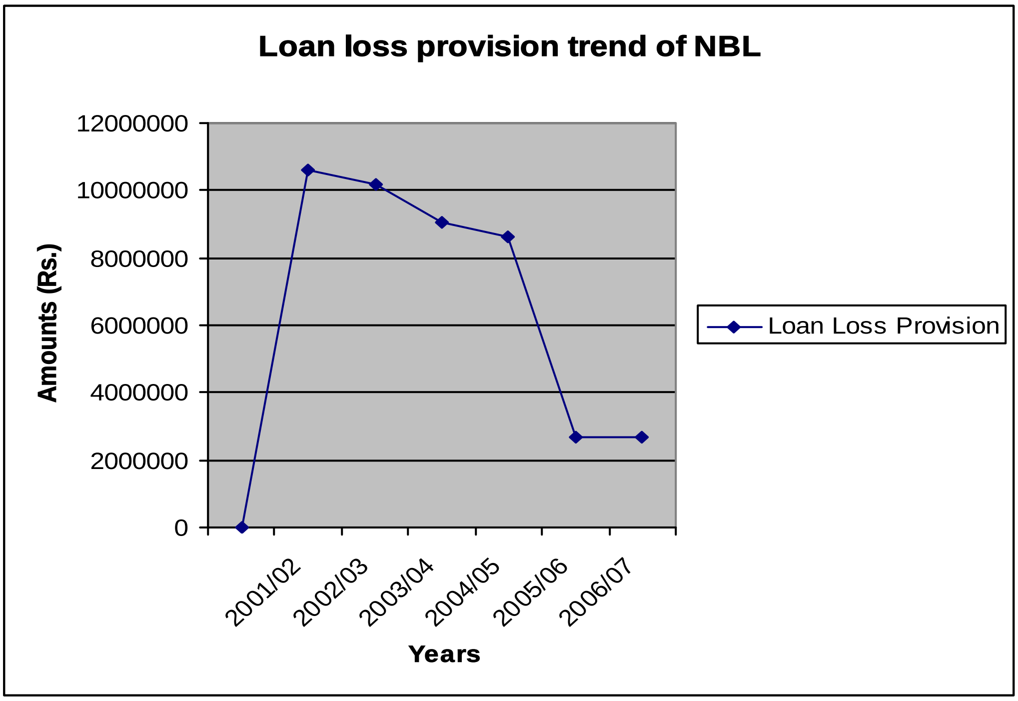
Loan loss provision trend of NBL

Table: 4.12

Loan loss provision trend of NBL

Rs. in 000

Year	Loan Loss Provision	Increase/(decrease)
2001/02	10,614,436	
2002/03	10,161,229	-4.27
2003/04	9,055,835	-10.88
2004/05	8,647,636	-4.51
2005/06	2,685,391	-68.95
2006/07	2,698,142	0.47
Average	33,248,233	-17.63



The above table shows the Loan Loss provision trend of NBL from the fiscal year 2002/03 to 2006/07. In the first four fiscal years the Loan Loss Provision is decreased and increased in last fiscal year of the study period. The highest decrease is In fiscal year 2005/06 i.e. 68.95% in the comparison of fiscal year 2004/05 and increase is 0.47% in fiscal year 2006/07 in the comparison of fiscal year 2005/. The average Loan Loss provision over the five fiscal year is Rs.33,248,233 thousand and average decrease loan loss provision is 17.63% in comparison of the subsequent fiscal year.

CHAPTER - FIVE

SUMMARY, CONCLUSION & RECOMMENDATION

5.1 Summary

In this chapter, summary, conclusion and recommendation are included. We have done effect of non-performing assets on profitability of Nepal Bank Limited by using financial as well as statistical tools.

This concluding chapter deals with the findings in a logical and rational manner to the problems of research within the framework stated in introduction chapter. This chapter is also related with the findings and conclusions derived from the study of the big and oldest bank. This chapter is composition of the study and some practical recommendations are suggested to solve the problems observed on the basis of findings, which would be beneficial for the management of the bank and concerned persons.

The first chapter consists of framework of the study as well as profile of Nepal Bank Limited. Similarly, second chapter is good review of the issues related with Non-performing Assets on the Performance of NBL. Techniques are briefly reviewed in the third chapter under the heading of research methodology. Fourth chapter consists of analytical framework of data and findings that is considered as the important part revealing the performance of the Bank.

Based on the presentation, Interpretation and analysis of data the major findings are summarized as follows:

1. The Average Loan and Advance is Rs.15, 826,941 thousand, Average Deposit is Rs.36, 305,436 thousand and Average Loan and Advance to Total Deposits Ratio is 43.59% in the study period.

2. The Average Non- performing Assets is Rs.6, 619,067. Thousand, Average Loan and Advance is Rs.15, 826,941 thousand and the Average NPA to Loan and Advance Ratio is 39.11%.

3. The Average Non-performing assets is Rs.6,619,067 thousand, Average

Total Assets is Rs.206,201,224 thousand and Average NPA to Total assts Ratio is 15.64 %.

4. The Average Loan Loss Provision is Rs.6,649,647 thousand, Average Non-Performing assets is Rs.6,619,067 thousand and Average Loan Loss provision to NPA Ratio is 110.80%.

5. The Average Return is Rs.724,602 thousand, Average Assets is Rs.206,201,224 thousand and Average Return on Total assts Ratio is 1.757%.

6. The Average Net Profit is Rs.724,602 thousand, Average Shareholder's Equity is Rs.380,383 thousand and Average Return on Shareholders Equity is Rs.190.49 .

7. The average Non Performing assets to Net Profit ratio of Nepal Bank Ltd. are 913.48 times.

8. The Correlation Coefficient between Total Loan and Advances and Non-performing Assets of Nepal Bank Ltd. is 0.97

9. The Total Deposits of Nepal Bank Ltd. is in increasing trend except in fiscal year 2005/06 and the increasing ratio is 2.68.

10. The Total Loan and Advance of Nepal Bank Ltd. is in decreasing trend except in fiscal year 2006/07. The average decreasing ratio is 5.71.

11. The Non-performing Assets of Nepal Bank Ltd. is in decreasing trend except in fiscal year 2002/03 and the average decreasing ratio is 22.99.

12. Lastly, the Loan loss provision of Nepal Bank Ltd. is also in decreasing trend except in fiscal year 2006/07 and the decreasing ratio is 17.63.

5.2 Conclusions

The role of money in an economy is very important. Proper and well planned management of money directs, determines and enhances the health and productivity of total financial sector and the performance of the financial sector affect the growth of the economy. Hence, money is the subject to manage and banks are the manager thereof. Bank, as a manager collects, disperses and controls the flow of money. Banks collect the fund from public who has savings and disperse the fund to the person who is in need of it. In this ways, whole infrastructure of national development, direction of economy, rate of progress and even the habit of people is the functions of banking system. Therefore, the existence of a bank is for the change in every aspect of human beings and its presence is for the upliftment of people.

The oldest bank of Nepal, Nepal Bank Limited was established on 1994 B.S. Kartik 30, Monday (November 15, 1937) NBL's authorized capital was Rs.10 million & issued capital Rs. 2.5 million of which paid-up capital was Rs.842 thousand with 10 shareholders. It is the first bank of Nepal established under the principle of Joint venture (Joint venture between govt. & general public). It's vision is to remain the leading financial institution of the country.

NPA may be defined broadly as the Bad Debt. However NPA in terms of banking sector consists of those loans and advances which are not performing well and likely to be turn as bad loan. NPA as per current directives of Nepal Rastra Bank (NRB) has been categorized as classified loans and Advance. NPA has severe impacts on the financial institution. On the one hand, the investment becomes worthless as expected return can not be realized and on the other hand, due to the provisioning required for the risk mitigation, the profitability is directly affected. The existence of the bank can be questioned on this situation. Thus interest along with principle has to be recovered timely and without any obstacles.

Many joint venture Banks (JVBs) are operating in Nepal as commercial and Merchant Banks. The growth is still going on as many new banks are coming into existence after this study. JVBs are operating with higher technology and new efficient method in banking sector. But this study has been undertaken only in Nepal Bank Limited to examine and evaluate the NPA condition. Besides, latest financial statements of five years from 2001/02 to 2006/07 have been conferred for the purpose of the study. This study has been mainly conducted on the basis of secondary data that are processed and analyzed

NBL is not able to utilize the total deposit collected from its depositors in full phase because of economic and political situation of the country as well as low investment opportunities. The average loan & advance to total deposit ratio is 43.59% over the study period.

The Non-performing asset in NBL is not in acceptable level. Non-performing assets to total Loan and advances ratio is 39.11% and but it is decreasing continuously in the following years for the study period. Non-performing Assets to Total Assets ratio of NBL is high, i.e. 15.64 % in aggregate which denotes that NBL has a high amount of NPA and is not used the fund efficiently.

5.3 Recommendations

Based on the above analysis and major findings deduced from the study of impact of non-performing assets with respect to NBL, the following suggestions on behalf of the banks as:

1. NBL should invest in less risky investment sectors and more profit generating sectors, i.e. in productive sectors.
2. NBL need to bring newer scheme to mobilize its higher amount of deposits in extending credit.
3. It should make effort in order to minimize non-performing credits. Make credit policy more transparent, standard, and less risky and increase the quality of credit.
4. Increase Profitability by investing in more profitable sectors and by increasing the quality of extended credits. NBL should investigate thoroughly the wide range of investment opportunities in the market in order to improve profitability situation.
5. As formation of price is very complex process, some extremely outstanding sectors such as management efficiency, profitability status, future perspective, Bank's investment strategy, etc. should be improved immediately.
6. There is direct effect of NPA on profitability but inversely. That means increase in NPA increases the profitability of bank because of loan loss provision. Therefore banks should minimize it's NPA level to increase their profitability.

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APPENDIX - I

नेपाल बैंक लिमिटेड

२०६० साल अषाढ ३२ गतेको वासलात

पुँजी र दायित्व					
गत वर्ष रु.	विवरण	अनुसूची	यस वर्ष रु.	गत वर्ष रु.	
३८०,३८२,६००।००	१. शेयर पुँजी	१	३८०,३८२,६००।००	१,६६५,१०३,६६५।११	१.
(९,९३४,२५८,२१३।९०)	२. जगेडा तथा कोषहरु	२	(१०,२११,५१४,३०१।६६)	४,९६२,०१२,०५९।३६	२.
२१३,२६३,५७३।०९	३. तिर्न बाँकी कर्जा सापट	३	५२,००९,९३५।८८	१,५४३,५९९,०७८।८४	३. अल्प हुने
३४,२६४,८४६,०६१।७९	४. निक्षेप हिसाब	४	३५,०१४,००१,४४३।८८	७,१५१,३८१,५८१।३२	४.
१२०,१४५,१७४।९५	५. भुक्तानी दिनु पर्ने बिलहरु	५	१४१,३११,३५६।७९	८,६३८,४३८,१५९।३७	५. बिल
१४,५१५,४६३,४२३।०४	६. अन्य दायित्व	६	१४,४४०,२९९,४६९।२५	१३९,६४०,५६८।९२	६.
				१५,४५९,६६७,५०६।०५	७.
३९,५५९,८४२,६१८।९७	कुल दायित्व :		३९,८१६,४९०,५०४।१४	३९,५५९,८४२,६१८।९७	

सम्भाबित दायित्व अनुसूचि १४
संचालकहरुको Declaration अनुसूचि २३
पुँजीकोषको पर्याप्तता अनुसूचि २४
प्रमुख सुचाङ्कहरु अनुसूचि २५
नगद प्रवाह विवरण अनुसूचि २६
प्रमुख लेखा नीतिहरु अनुसूचि २७
लेखा सम्बन्धी टिप्पणीहरु अनुसूचि २८
१ देखि १४ सम्मको अनुसूचीहरु बासलातका अभिन्न अङ्ग हुन् ।
मिति : पौष २५, २०६०

APPENDIX - II

नेपाल बैंक लिमिटेड

मिति २०५९ श्रावण १ गते देखि २०६० आषढ ३२ गते सम्मको नाफा नोक्सान हिसाब

खर्च					
गत वर्ष रु.	विवरण	अनुसूची	यस वर्ष रु.	गत वर्ष रु.	विवरण

१,७१३,२०२,६७९।१०	१. व्याज खर्च	१५	१,५८५,५९९,८४५।०३	१,५२६,९८९,०३४।११	१. व्य
१,२२७,८५१,१७८।२०	२. कर्मचारी खर्च	१६	१,५४१,८२८,९६९।१२	२४१,००६,५३३।८६	२. क डिष्का
१५८,४९१,६८६।३४	३. कार्यालय संचालन खर्च	१७	२२५,९२३,१७६।६९	१८३,६१९,९४८।१६	३. स आम्दा
-	४. सटही घटवढ नोक्सान	२०	-	१२४,७५८,७८५।२६	४. गै आम्दा
-	५. गैर संचालन खर्च	२१	-	६६,३११,१९४।०५	५. अ
-	६. असुली हुन नसक्ने कर्जाको अपलेखन		-	३,०७१,२९६,०४८।२०	६. खु सारेको
२,११४,४३६,०००।००	७. जोखिम सम्बन्धी व्यवस्था		-		
-	८. कर्मचारी बोनस व्यवस्था		-		
-	९. आयकर व्यवस्था		-		
-	१०. लगानीमा व्यवस्था		१६,२९०,०००।००		
-	११. खुद नाफा (तल सारेको)		-		
५,२१३,९८१,५४३।६४	**जम्मा :**		**३,३६९,६४१,९९०।८४**	**५,२१३,९८१,५४३।६४**	

गत वर्ष रु.	विवरण	यस वर्ष रु.	गत वर्ष रु.	
७,३८१,१४८,८६४।५५	१. गत वर्षसम्मको संचित नोक्सान	१०,६३६,०८६,०९८।८३		
३,०७१,२९६,०४८।२०	२. यस वर्षको नोक्सान	२५१,७३०,६७२।०६	-	१. ग संचित
-	३. साधारण जगेडाकोष	-		
-	४. भैपरी आउने जगेडा	-	-	२. य
-	५. बैंक विकास कोष	-		
-	६. लाभांश समीकरण कोष	-	१०,६३६,०८६,०९८।८३	३. स
-	७. कर्मचारी सम्बन्धी जगेडाहरु	-		
-	८. अन्तरिम एवं प्रस्तावित लाभांश	-		
-	९. बोनस शेयर जारी	-		
-	१०. विशेष जगेडा कोष	-		
४२,९३८,१८६।०८	११. सटही घटवढ कोष	-		
	१२. आयकर भूक्तानी (	-		

१४०,७०३,०००।००	आ.ब.२०५४।५५ सम्मको)			
	१३. सञ्चित मुनाफा	-		
१०,६३६,०८६,०९८।८३	**जम्मा:**	**१०,८८७,८१६,७७०।८९**	**१०,६३६,०८६,०९८।८३**	**जम्म**

१५ देखि २२ सम्मका अनुसूचीहरु नाफा नोक्सान हिसाबका अभिन्न अङ्ग हुन् ।
मिति : पौष २५, २०६०

APPENDIX - III

नेपाल बैंक लिमिटेड

२०६२ साल आषाढ ३१ गतेको वासलात

पुँजी र दायित्व					
गत वर्ष रु.	**विवरण**	**अनुसूची**	**यस वर्ष रु.**	**गत वर्ष रु.**	**विवरण**
३८०,३८२,६००	१. शेयर पुँजी	१	३८०,३८२,६००	१,०१०,२३१,४६७	१. नगद
ढ९,३९४,९०८,४९१ण	२. जगेडा तथा कोषहरु	२	ढ७,८०५,९२८,४८९ण	४,८५०,८३८,८९५	२. बैंक
(	३. तिर्न बाँकी कर्जा सापट	३	१,२४७,०६५,३७४	७५१,९९४,५२१	३. माग प्राप्त हु
३५,७३५,०४४,४२७	४. निक्षेप हिसाब	४	३५,९३४,१६३,६४५	११,००४,८१९,५७१	४. लग
३१,४२६,६३५	५. भुक्तानी दिनु पर्ने बिलहरु	५	४१७,७८७,८५६	८,८८१,८२३,३२३	५. कर्ज खरिद
१७,४०९,९३४,८६४	६. अन्य दायित्व	६	१६,८७१,६८३,००५	१९५,०४६,५०८	६. स्थिर
				१७,४६७,१२५,७५०	७. अन्य
४४,१६१,८८०,०३५	**कुल दायित्व :**		४७,०४५,१५३,९९१	४४,१६१,८८०,०३५	**कुल**

सम्भाबित दायित्व अनुसूचि १४
संचालकहरुको Declaration अनुसूचि २३
पुँजीकोषको पर्याप्तता अनुसूचि २४
प्रमुख सुचाङ्कहरु अनुसूचि २५
नगद प्रवाह विवरण अनुसूचि २६
प्रमुख लेखा नीतिहरु अनुसूचि २७
लेखा सम्बन्धी टिप्पणीहरु अनुसूचि २८

मिति : मार्ग १२, २०६२
१ देखि १४ सम्मको अनुसूचीहरु बासलातका अभिन्न अङ्ग हुन् ।

APPENDIX - IV

नेपाल बैंक लिमिटेड

मिति २०६१ श्रावण १ गते देखि २०६२ आषढ ३१ गते सम्मको
नाफा नोक्सान हिसाब

खर्च					
गत वर्ष रु.	विवरण	अनुसूची	यस वर्ष रु.	गत वर्ष रु.	विवरण
१,०२५,५३२,७८९	१. व्याज खर्च	१५	७४८,९५२,६१७	१,८२५,०४१,४२१	१. व्याज अ
१,८४८,८४५,८१७	२. कर्मचारी खर्च	१६	१,३०५,२४९,२६५	२३१,९१५,६२४	२. कमिशन
३१७,५८१,९०६	३. कार्यालय संचालन खर्च	१७	३८२,७१०,५५९	७१,८१५,०११	३. सटही घ
	४. सटही घटवढ नोक्सान	२०	-	६४५,५२८,४६९	४. गैर संच
	५. गैर संचालन खर्च	२१	-	१,२०६,९८४,२५३	५. अन्य अ
	६. असुली हुन नसक्ने कर्जाको अपलेखन		-	-	६. खुद नोक
-	७. जोखिम सम्बन्धी व्यवस्था		-		
५००	८. लगानीमा व्यवस्था		४,२५०,०००		
७८,९३२,३७७	९. कर्मचारी बोनस व्यवस्था		-		
-	१०. आयकर व्यवस्था		-		
७१०,३९१,३८९	११. खुद नाफा (तल सारेको)		१,७३०,१२९,७००		
३,९८१,२८४,७७८	**जम्मा :**		**४,१७१,२९२,१४१**	**३,९८१,२८४,७७८**	**जम्मा :**

गत वर्ष रु.	विवरण	यस वर्ष रु.	गत वर्ष रु.	विवरण
१०,८८७,८१६,७७१	१. गत वर्षसम्मको संचित नोक्सान	१०,३३२,०६९,३७४		१. गत वर्ष मुनाफा
	२. यस वर्षको नोक्सान	(		
	३. साधारण जगेडाकोष			

१४२,०७८,२७८		३४६,०२५,९४०		
	४. भैपरी आउने जगेडा	-	७१०,३९१,३८९	२. यस वर्ष
	५. बैंक विकास कोष	-		
	६. लाभांश समीकरण कोष	-		
	७. कर्मचारी सम्बन्धी जगेडाहरु	-		
	८. अन्तरिम एवं प्रस्तावित लाभांश	-	१०,३३२,०६९,३७४	३. सञ्चित
	९. बोनस शेयर जारी	-		
	१०. विशेष जगेडा कोष	-		
१२,५६५,७१४	११. सटही घटवढ कोष	-		
	१२. आयकर भूक्तानी	-		
	१३. पूजी मिलान कोष	७६,०७६,५२०		
	१३. सञ्चित मुनाफा	-		
११,०४२,४६०,७६३	**जम्मा :**	**१०,७५४,१७१,८३४**	**११,०४२,४६०,७६३**	**जम्मा :**

१५ देखि २२ सम्मका अनुसूचीहरु नाफा नोक्सान हिसाबका अभिन्न अङ्ग हुन् ।
मिति : मार्ग १२, २०६२

7.