CHAPTER – I
INTRODUCTION

1.1 Background of the Study

Bank plays a vital role to encourage thrift and discourage hoarding by mobilizing the resources and removing the habit of hoarding. They pursue economic growth rapidly, developing the banking habit among the people by collecting the small-scattered resources in one bulk, using them in the further productive purposes, and rendering other valuable service to the country. Thus, this gives the individual an opportunity to borrow funds against future income, which may improve the economic well being of the borrower.

Bank deals with the offer of collected deposits and provides the loan for commercial purpose. In other words, bank facilities act as right hand for the growth of trade and industry for national economy of developing country like Nepal. The above fact shows that a bank plays vital role for the economic development of the country. Commercial banks play an important role for economic development of nation. They have adopted new banking technique, management like, hypothecation, syndication lending polices, tele-banking credit card, master card from international banking technique. They render various services to their customers in order to facilitate their economic and social life. Commercial banks are operating in Nepal in an act as commercial banks are operating and performing their work under the direction of Nepal Rastra Bank. Nowadays, there are many Commercial banks and other financial institutions, but there are little opportunities to make fair investment. Meanwhile, the banks and financial institutions are offering very low deposit and credit interest rate. So to survive in the competitive banking market, one should follow the fundamental principles of sound investment policy with minimum risk and maximum profit. At present, more than three dozens of the Commercial banks are operating in Nepal and are playing important role in the economic development of the country.

Investment policy is an important ingredient of overall national economic development because it ensures efficient allocation of fund to achieve the materials and economic well being of the society as a whole. In this regard, Commercial bank investment policy push drives to achieve priority of commercial sectors in the context of Nepal's economic development. National development of any country depends upon the economic development of that country and economic development is supported by financial infrastructure of that country. Banks constitute an important segment of financial infrastructure of any country. Banking when properly organized it aids and facilities the growth of trade and industry and hence of national economy. In the modern economy, banks are to be considered not as dealers in money but as the leaders of development.

Banking plays a significant role in the development of nations. Bank is a financial institution which primary classes in borrowing and lending. Modern bank prefers varieties of functions. Therefore it is difficult to decide the function of a modern bank because of their complexity and versatility in operation. Various authors have defined the word 'Bank' in different ways. A commercial bank is dealer in money and it substitutes for money such as cheque or bills of exchange, it also provides a variety of financial service.

Commercial banks are major financial institution, which occupy quite important place in the framework in every economy because they provide capital for the development of industry. Commercial banks formulate sound investment policies to make it more effective, which eventually contribute to the economic growth of country. The bound policies help commercial banks maximizing quality and quantity of investment and hereby achieve the own objective of profit maximization and social welfare. Formulation of sound investment policies and co-ordinate and planned efforts pushed forward the forces of economic growth.

In the study, the word investment conceptualized the investment of income, savings or other collected fund. The term investment covers a wide range of activities. It is commonly known fact that an investment is only possible where there is adequate saving. If all the incomes and savings are consumed to solve the problem of hand to mouth and to the other basic needs. Then there is no existence of investment. Therefore, both saving and investment are interrelated. Investment policy is an important ingredient of overall national economy development because it ensures efficient allocation of fund to achieve the materials and economic well being of the society as a whole. In this regards, commercial bank investment policy push drives to achieve priority of commercial sectors in the context of Nepal's economic development.

1.1.1 Profile of the Selected Banks

a) Everest Bank Limited

Everest Bank Limited (EBL) started its operations in 1994 with a view and objective of extending professionalized and efficient banking services to various segments of the society. The bank is providing customer-friendly services through its Branch Network. All the branches of the bank are connected through Anywhere Branch Banking System (ABBS), which enables customers for operational transactions from any branches. Moreover, EBL was one of the first bank to introduce Any Branch Banking System (ABBS) in Nepal.

In addition, EBL has introduced Mobile Vehicle Banking system to serve the segment deprived of proper banking facilities through its Birtamod Branch, which is the first of its kind. EBL has introduced branchless banking system first time in Nepal to cover unbanked sector of Nepalese society. EBL is first bank that has launched e-ticketing system in Nepal. EBL customer can buy yeti airlines ticket through internet. With an aim to help Nepalese citizens working abroad, the bank has entered into arrangements with banks and finance companies in different countries, which enable quick remittance of funds by the

Nepalese citizens in countries like UAE, Kuwait, Bahrain, Qatar, Saudi Arabia, Malaysia, Singapore and UK.

b) Nepal Investment Bank Limited

Nepal Investment Bank Ltd. (NIBL), previously Nepal Indosuez Bank Ltd., was established in 1986 as a joint venture between Nepalese and French partners. The French partner (holding 50% of the capital of NIBL) was Credit Agricole Indosuez, a subsidiary of one the largest banking group in the world. With the decision of Credit Agricole Indosuez to divest, a group of companies comprising of bankers, professionals, industrialists and businessmen, has acquired on April 2002 the 50% shareholding of Credit Agricole Indosuez in Nepal Indosuez Bank Ltd.

The name of the bank has been changed to Nepal Investment Bank Ltd. upon approval of bank's Annual General Meeting, Nepal Rastra Bank and Company Registrar's office with the shareholding structure of 50% capital by a group of companies, 15% capital by Rastriya Banijya Bank, 15% capital by Rastriya Beema Sansthan and 20% being held by the General Public.

NIBL, which is managed by a team of experienced bankers and professionals having proven track record, offers what one is looking for. The bank ensures that one's choice of a bank will be guided among other things by its reliability and professionalism. The vision of the bank is to be 'the most preferred provider of Financial Services in Nepal.

1.2 Statement of the Problem

In developing countries, the contribution on industrial sector is also very low in the output and the employment. In Nepal the commercial bank has played a catalytic role in the economic growth. Its investment range from small-scale cottage industries to large industries making investment in loans and government securities one may always wonder which investment is better. It

can be hypothesized that bank portfolio variables like loans, investment, cash reserve, deposit and borrowing affects the national income and also how the government policy affects these variables, such as the effect of an interest rate on the bank portfolio variables is of great concern, therefore when monitoring money and credit conditions, the central bank has to keep an eye on the bank portfolio behavior. Nepalese commercial banks have not formulated their investment policy in an organized manner. They mainly rely upon the instructions and guidelines of Nepal Rastra Bank. They do not have clear view towards investment policy. Furthermore the implementation of policy is not in an effective way.

Thus the present study will make a modest attempt to analyze investment policy of Everest Bank Limited (EBL) and Nepal Investment Bank Limited (NIBL). In this study, EBL investment policy is analyzed comparing it with NIBL. Following are the major problems that have been identified for the purpose of this study.

a. What portion of the total assets does the investment of the bank covers?
b. On which sector, government securities, shares and debentures & interbank lending, does the bank give preference while making investment?
c. What return have been obtained by EBL and NIBL from investment and what is the investment loss provision?
d. What should the bank do for having optimum investment policy?

1.3 Objectives of the Study

The main objective of this study is to examine investment policy of EBL and NIBL. The specific objectives of the study are as follows:

a. To measure the utilization of total assets in making investment.
b. To analyze the investment in each sector, i.e. in government securities, corporate shares and debentures and interbank lending.

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c. To evaluate the return on investment in government securities, corporate shares and debentures and interbank lending?

d. To estimate the value of total investment and net profit in the future.

e. To collect the opinions of bank related personnel for the improvisation essential for having optimal investment policy.

1.4 Significance of the Study

The better the investment policy, the more valuable the company, the higher return to share holders etc. and vice versa. Since the different parties, shareholders, general public and government are directly affected by the investment policy of the financial institutions. The researcher feels the needs to study this policy effects on the management of banks, financial institution, shareholder, general public (customer, depositors and creditors), and other related parties. Nepalese commercial banks have not formulated their investment policy in an organized manner. They mainly depend upon the instructions and guidelines of NRB. They do not have clear view towards investment policy. Further more, the implementation of policy is not in an effective way. Thus the present study will make a modest attempt to analyze investment policy of EBL and NIBL. This study will provide a useful feedback for academic institution, bank employees, trainees, investors, for financial person, policy making bodies and other concerned people with bank.

1.5 Limitations of the Study

The followings are the limitation of the study:

a. The study analyzes only the financial investment, and hence real investment and other financial aspects have been ignored.

b. This study covers only a five year period i.e. from 2005/06 to 2009/10.

c. Only two banks, Everest Bank Limited and Nepal Investment Bank Limited, are taken for this study.

d. The accuracy of secondary data totally depends on the published annual reports of the banks' annual report, different publication, website and journals.

e. Similarly, the reliability of primary data absolutely depends on the opinions of the respondents.

1.6 Organization of the Study

The study will be divided into five chapters:

Chapter I: Introduction

This chapter deals with subject matters consisting of the background, statement of the problem, objectives, significance and limitation of the study.

Chapter II: Review of Literature

This chapter deals with review of various literatures of the study field within the framework, of which this research is conducted. Therefore, it includes conceptual framework along with the review of major journals, research works and thesis etc.

Chapter III: Research Methodology

This chapter deals with research methodology and includes the research design, population and sample, nature and sources data collection and data analysis tools.

Chapter IV: Data Presentation and Analysis

This chapter consists of an analysis and interpretation of the data, using financial tools and statistical tools as described in chapter three. Similarly this chapter also includes the major findings of the study.

Chapter V: Summary, Conclusion and Recommendations

This chapter summarizes and concludes the research work. Lastly, appropriate recommendations are made at the end of the chapter.

At the end of the study, Bibliography and Appendices are presented.

CHAPTER – II
REVIEW OF LITERATURE

2.1 Conceptual Review

2.1.1 Meaning of Investment

An investment involves the choice by an individual or an organization such as a pension fund, after some analysis or thought, to place or lend money in a vehicle, instrument or asset, such as property, commodity, stock, bond, financial derivatives (e.g. futures or options), or the foreign asset denominated in foreign currency, that has certain level of risk and provides the possibility of generating returns over a period of time. When an asset is bought or a given amount of money is invested in the bank, there is anticipation that some return will be received from the investment in the future. Investment is a term frequently used in the fields of economics, business management and finance. It can mean savings alone, or savings made through delayed consumption. Investment can be divided into different types according to various theories and principles. While dealing with the various options of investment, the defining terms of investment need to be kept in mind. *(Bodie & Merton; 2002: 202-203)*

The word 'investment' can be defined in many ways according to different theories and principles. It is a term that can be used in a number of contexts. However, the different meanings of investment are more alike than dissimilar. Generally, investment is the application of money for earning more money. Investment also means savings or savings made through delayed consumption. *(Ross; 2002: 78)* According to business theories, investment is that activity in which a manufacturer buys a physical asset, for example, stock or production equipment, in expectation that this will help the business to prosper in the long run. Investment is the commitment of money or capital to purchase financial instruments or other assets in order to gain profitable returns in the form of interest, income, or appreciation of the value of the instrument. Investment is related to saving or deferring consumption. *(Musiela & Rutkwoski; 1998: 665)*

According to economics, investment is the utilization of resources in order to increase income or production output in the future. An amount deposited into a bank or machinery that is purchased in anticipation of earning income in the long run is both examples of investments. Although there is a general broad definition to the term investment, it carries slightly different meanings to different industrial sectors. *(Duffie; 2001: 51)* According to economists, investment refers to any physical or tangible asset, for example, a building or machinery and equipment.

On the other hand, finance professionals define an investment as money utilized for buying financial assets, for example stocks, bonds, bullion, real properties, and precious items. According to finance, the practice of investment refers to the buying of a financial product or any valued item with anticipation that positive returns will be received in the future. The most important feature of financial investments is that they carry high market liquidity. The method used for evaluating the value of a financial investment is known as valuation. *(Musiela & Rutkwoski; 1998: 65)*

Investment in Terms of Business Management

According to business management theories, investment refers to tangible assets like machinery and equipments and buildings and intangible assets like copyrights or patents and goodwill. The decision for investment is also known as capital budgeting decision, which is regarded as one of the key decisions. *(Tuckman; 2002: 15)*

Investment in Terms of Economics

According to economic theories, investment is defined as the per-unit production of goods, which have not been consumed, but will however, be used for the purpose of future production. Examples of this type of investments are tangible goods like construction of a factory or bridge and intangible goods like 6 months of on-the-job training. In terms of national production and income,

Gross Domestic Product (GDP) has an essential constituent, known as gross investment. *(Clewlow & Strickland; 1998: 315)*

Investment in Terms of Finance

In finance, investment refers to the purchasing of securities or other financial assets from the capital market. It also means buying money market or real properties with high market liquidity. Some examples are gold, silver, real properties, and precious items. Financial investments are in stocks, bonds, and other types of security investments. Indirect financial investments can also be done with the help of mediators or third parties, such as pension funds, mutual funds, commercial banks, and insurance companies. *(Tuckman; 2002: 17)*

2.1.2 Types of Investment

A particular investor normally determines the investment types after having formulated the investment decision, which is termed as capital budgeting in financial lexicon. With the proliferation of financial markets there are more options for investment types. According to the financial terminology investment means the following:

- Purchasing Securities in Money or Capital Markets
- Buying Monetary or Paper Financial Assets in Money or Capital Markets
- Investing in Liquid Assets like Gold, Real Estate and Collectibles

Investors assume that these forms of investment would furnish them with some revenue by way of positive cash flow. These assets can also affect the particular investor positively or negatively depending on the alterations in their respective values. *(Questa; 1999: 13)*

A) Share Market Investment

Shares are purchased and sold on the primary and secondary share markets. To invest in the share market, investors acquire a call option, which is the right to

buy a share, or a put option, which is the right to sell a share. In general, investors buy put options if they expect prices to rise, and call options if they expect prices to fall. For currency rate exchanges, investors may buy a swap option.

The value of a derivative depends on the value of the underlying asset. The various classifications of derivatives relevant to share market investment are:

- Swap
- Futures Contract
- Forward Contract
- Option Contract *(Questa; 1999: 23)*

Before a share is chosen for investment, a technical analysis of the share is performed. The price and volume of a share over a period of time are tracked and then a business plan is constructed. A fundamental analysis involves a close study of the company associated with the share, and its performance over time. The fundamental analysis is important for the share market investor.

B) Land Investment

Land as investment is a long-term investment and as the price of land all over the world has taken an upswing, this form of investment can be termed as a safe bet. Big development companies, wealthy individuals and well-off farmers have involved themselves in land investment. However, a system for efficient development of land must be in place. With the increase in land prices, investment in land can be very lucrative as capital gains are easily realized. Besides, land is a tangible asset and the investors can use it in their best interests.

Land investment forms a major part of real estate investment. The attachments to lands and buildings are not an essential requirement of land investment and it is the main point of difference between land investment and real estate

investment. Land can be termed as the most basic form of asset. The land developer is entrusted with the duty of developing the land. Land appreciates in value with establishment of buildings and other proper amenities on it. *(Pattillo; 1998: 530-531)*

C) Capital Investment

Capital investment is defined as the expenditure that may be incurred by a business organization in order to purchase machineries and other fixed assets. This expenditure is normally beneficial as it lays the foundation for future investments of similar kind. Capital spending is normally performed for categories that are expected to last for more than a single year. The value of the assets being bought with capital spending is supposed to be important as far as the preparation of the cash flow statement is concerned.

As per the capital investment plans, the companies spend primarily on buying new plants or equipments that may be related to their field of work. Nowadays, the number of investors willing to opt for the medium of capital investment is on the rise. The phenomenon of working capital is relevant in the context of capital investment as well as determining a company's operational status. The efficacy of operations of a company is normally inversely proportional to the building up of working capital. Methods like Net Present Value and Internal Rate of Return are employed when the proposals for venture capital investments are judged. *(Hull; 2002: 35-36)*

D) Financial Market Investment

When investing in the financial market, traders are provided with the opportunity to deal in financial securities, commodities and other freely interchangeable goods at affordable rates of transaction. The prices of these are reflective of effective market speculation. It has been observed that there has been noticeable evolution and an increase in the various financial markets.

These markets are making the best of efforts to enhance the factor of liquidity. The different financial markets that are available at the present time are:

- Real Estate Market
- Bond Market
- Commodities Market
- Stock or Equities Market
- Spot or Cash Market
- Forex Market
- Over-the-counter Market
- Derivatives Market *(Gould; 1968: 50)*

There is an existence of general, as well as specialized financial markets in today's world. General markets are where a diverse group of commodities are traded, whereas specialized ones are those, which specialize in dealing with only one kind of commodity or good.

The financial markets of today bring buyers with different interests onto the same platform. This process enables them to locate prospective customers and enhances the efficiency of the market operations as a whole.

E) Stock Investment

The process of stock investment enables the stock traders or investors to trade in securities. Investors can operate individually or under the guidance of investment management companies. The system of stock investment is not devoid of prices and the process involves a considerable amount of risk and uncertainty. The ones who are most likely to be affected by the harsh nature of the stock investment are the new investors and those who are not wise in their decision making process. *(Hull; 2002: 41)*

It could be assumed safely that stock market investment is definitely not the right option if an investor is interested in making quick money. While investing

in the stock market it is usual for the investors and the traders to be confronted with expenses like the following:

) Commissions
) Fees to be Paid for Brokerage and other Services
) Taxes

F) Retirement Investment

Retirement investment planning ensures financial security in the post retirement period. The resulting retirement benefits prove to be of great use for retirees. A considerable amount of money should be invested in retirement investment plans. Money must not be withdrawn indiscriminately from retirement accounts. An individual's various retirement investments must be monitored regularly. Both social security and investment in stocks may contribute to an individual's retirement.

The first step to success in retirement investing is to develop the habit of saving early in life. Next, a sound investment strategy is necessary, one which allows for an amount of risk but also enhances the average annual returns on investment. Investment in short-term government bonds and government treasury bills are two examples of areas for retirement investment. *(Questa; 1999: 28)*

G) Real Estate Investment

Real estate can broadly be defined as immovable property. Land and things attached to it in permanence, such as buildings, come under the category of real estate. Investment in real estate has its fair share of risks. But one advantage of real estate is that it gives the owner the right to transfer the title to the land.

Real estate investors often own more than one unit of real estate. The investor uses one unit as his or her residence and accrues rental income from the others. Investment in real estate also involves value appreciation of property over time,

which leads to capital gains. The whole program of real estate investment is a long-term process. *(Pattillo; 1998: 535)*

H) Gold Investment

Gold investment is a long-term investment scheme involving low risks. People willing to invest in gold have a natural advantage because the demand for gold is much more than its actual supply. The price of gold is generally in a continual rise. However, investors should not invest all their funds in one kind of gold investment. The gold industry is huge and has many facets, and a savvy investor can exploit this. Money can be invested directly in gold mines, for example, which can be more lucrative than investing in physical gold. *(Lucas; 1967: 81)*

Gold investors prefer to buy gold in its cheapest forms such as krugerrands, sovereigns and bars. Gold bars are the cheapest while gold sovereigns, because of their smaller size, are worth paying an extra premium for.

I) Portfolio Investment

Portfolio investment refers to the passive holdings of the financial securities such as foreign stocks, foreign bonds and other foreign financial assets, which are not under the control of the investors.

Unlike foreign direct investment, the issuers of securities do not control the portfolio investment. The foreign direct investment involves the investors to make investment to acquire the lasting interest in the enterprises that are operational outside the domestic economy. A typical foreign direct investment relationship allows the parent enterprise and a foreign affiliate to form together a transnational corporation.

The portfolio investments are primarily connected with the portfolio diversification process and the examples of portfolio investment are:

） Purchasing of shares in a foreign company

） Purchasing of bonds that is issued by a foreign government

） Acquisition of the assets in a foreign country. *(Cox & Ross; 1976: 148)*

The developing countries use the portfolio investment as a growing tool in the economy and take some measures to encourage the use of portfolio investment. While going for liberalization and economic reforms in order to bring about the substantial and rapid economic growth, the government takes up some policies and instruments. The portfolio investment is one of the most famous financial instruments that are taken up by government to enhance the economic growth. The foreign direct investments are also encouraged by the developing countries while going for the economic reforms. *(Lucas; 1967: 84)*

J) Business Investment

Business investment can give investors a chance to invest in different kinds of businesses. Business investment can be a good option for the investors to manage their own portfolios.

A number of business investment opportunities exist. Investors may choose from different business investment plans depending on the market conditions and trends. Business investment typically means purchasing an asset in the form of stocks or bonds with a hope of getting returns and interest in the future. Companies also release their shares and bonds in the capital market in order to collect money for some financial purpose. The assets that are purchased may be physical, intangible, or financial depending on the nature of the asset. *(Jarrow & Turnbull; 1999: 102-103)*

Business finance, on the other hand, refers to the business finance loan, which is one of the easiest ways to acquire funds for a company. Considering the cutthroat competition of the business world, having financial support seems to

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be crucial. Finance is the most important aspect for an entrepreneur both in order to start a new business and to expanding an existing business.

K) Equity Investment

Equity investment refers to the trading of stocks and bonds in the share market. It is also referred to as the acquisition of equity or ownership participation in the company.

An equity investment is typically an ownership investment, where the investor owns an asset of the company. In this kind of investment there is always a risk of the investor not earning a specific amount of money. Equity investment can also be termed as payment to a firm in return for partial ownership of that firm. An equity investor, in some cases, may assume some management control of the firm and may also share in future profits. *(Eisner & Strotz; 1963: 35-36)*

In order to understand equity investment properly, it is necessary to see the technical and fundamental analysis. The technical analysis of equity investment is primarily the study of price history of the shares and stock market. A fundamental analysis of equity investment involves the study of all available information that is relevant to the share market in order to predict the future trends of the stock market. The annual reports, industry data and study of the economic and financial environment are also included in the fundamental information of equity investment.

2.1.3 Best Investment

The best investment options depend on the particular investor. Two people cannot be the same and so, the definition of this 'best' is bound to vary from investor to investor. At the same time, the market conditions are also responsible for making an investment option good or bad. There are several factors, which are related to the definition of bet investment plan. These are:

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a) Safety

The safety of the investment is the basic factor for investing money. There are several types of risks, which are included in an investment. The prime risk is of facing huge loss. On the other hand the slow paced growth of the investment is also a matter of concern for the investors. So, the best investment should cover these factors. *(Flavell; 2002: 45)*

b) Return

Return is another matter of concern for the investors. There are several investment mediums, which promise low but safe return. On the other hand, the high yielding mediums are related to the high level of risk. Now this depends solely on the investor to identify the best investment option according to his or her mental set up.

Everybody wants to save some amount of money from the taxes. Now if the investments can do this for them, then it is surely going to be a lucrative option for them. It can also be considered as the best option if it can provide the above discussed factors with the tax relief. *(Flavell; 2002: 46)*

c) Investment Planning

The basic idea behind any form of investment planning is to maximize future financial returns for future security. In formulating a financial plan, an individual investor must carefully consider his or her choices before making any decision.

Investment planning involves considering many possible financial options that could be used to secure the desired financial future. Often groups of individuals get together for the purpose of investment planning.

Investment plans require careful scrutiny of the financial market. It is mostly the responsibility of the particular firm to make the decision on the matter of

management of money, which could be utilized in meeting long term asset investment plans or for gathering working capital.

An integral part of financial planning is the system a particular investor uses to decide how much and in what ways to invest. Another important task is to ascertain the source from where the money could be obtained.

Yet another important aspect of investment planning is analyzing the development and performance of investments in a particular span of time. This could help the investor by cutting down on the amount of uncertainty involved in the process. Investment planning also helps investors in channeling their funds in the right direction. *(Flavell; 2002: 48-50)*

2.1.4 Investment Strategy

Investment strategy is actually the plan, which is followed by an investor to make profits and to achieve financial stability. Based on this investment strategy the investor identifies the areas where the money can be invested safely. At the same time the returns from that money is also of equal importance. The investment strategy also helps the investor to reduce the risk factor from the investment portfolio. *(Das; 2002: 61)*

Now several investment options are available in the market. There are thousands of people who are making money from these options. Again, there are also a large number of investors who are facing losses every day. This means that if the investment is done in a proper manner, the profit can be made from every possible medium otherwise the result may be the opposite.

But to make the investment successful, an investor needs to do the homework properly. He or she needs to follow that market closely in which he or she wants to invest. There are several sources like the financial market news, several journals, internet and many more that can provide vital information

about the financial market. This information is very important to form a strategy. At the same time, the financial planners can also provide assistance to form an investment strategy, which suits the need of the investor.

Before planning a strategy for investment, one needs to be sure about the aim of his or her investment. One needs to decide about the desired returns and more importantly the amount of risk that he or she can bear. These factors are going to decide the suitable medium of investment for the investor.

The investment medium may be anything; the investment portfolio of the investor should be diversified. Investing in one single medium may increase the amount of risk. In multi-investment, the risks related to one medium are covered through another one. *(Das; 2002: 64)*

An essential of investment refers to why investment, or the need for investment, is required. The investment strategy is a plan, which is created to guide an investor to choose the most appropriate investment portfolio that will help him achieve his financial goals within a particular period of time. An investment strategy usually involves a set of methods, rules, and regulations, and is designed according to the exchange or compromise of the investor's risks and returns.

Investment strategies can be broadly categorized into the following types:

- Active strategies: One of the principal active strategies is market timing (an investor is able to move into the market when it is on the low and sell the stocks when the market is on the high), which is applied for maximizing yields.
- Passive strategies: Frequently implemented for reducing transaction costs.

One of the most popular strategies is the buy and hold, which is basically a long term investment plan. The idea behind this is that stock markets yield a commendable rate of return in spite of stages of fluctuation or downfall. Indexing is a strictly passive variable of the buy and hold strategy and, in this case, an investor purchases a limited number of every share existing in the stock market index, for example the Standard and Poor 500 Index, or more probably in an index fund, which is a form of a mutual fund.

Additionally, as the market timing strategy is not applicable for small-scale investors, it is advisable to apply the buy and hold strategy. In case of real estate investment the retail and small-scale investors apply the buy and hold strategy, because the holding period is normally equal to the total span of the mortgage loan. *(Das; 2002: 65-67)*

2.1.5 The Fundamentals of Investment Management

The fundamentals of investment management taken by the investment management companies include the processing of the securities and assets in such way so as to gain the maximum benefit for the client investors.

The client investor in the investment management may either be an insurance company, a corporation or a pension fund or even may be private investor going for collective investment schemes like mutual fund. The investment managers are sitting at the centre of all investment management taking all the decisions on behalf of the client's investments. The investment managers generally take the fundamentals of investment management only. The investment advisor makes an assessment on the needs and risk profile of each client.

One of the prime tasks of the investment management firms is to allocate the asset and the exercise of allocating funds among these assets is of high importance, while the classes of the assets being stocks, bonds, commodities

and real estate. The asset allocation carries significant effect on the performance of a fund as the different asset classes show different interaction effects and market dynamics, while some researches even suggest that the asset allocation are having the predictive power in fund's success. It is the prime task of the investment manager to allocate the asset in the most feasible way in order to ensure the success of the fund. *(Brealey, Razavi & Myers; 2002: 71-72)*

The diversification is another measure that the investment managers take up seriously after asset allocation. The managers construct a list of planned holding depending on the theory of portfolio diversification and the list eventually indicates the amount or percentage that the fund should invest in a particular bond or stock.

A number of different styles of fund management are available that an investment management institution can take up while growth, market neutral, value, indexed, small capitalization, etc being the examples. Every style of fund management has its own distinctive adherents and features while in any particular financial environment it shows distinctive risk characteristics. The performance of the fund is the main acid test for fund management firms and managers. In order to make the performance measurement accurate, all the financial institutions measure the performance of each fund and also get it measured by external performance measurement firms. The aggregate industry data showing how the funds performed against some given indices over various time periods is the main index for performance measurement of a fund. *(Brealey, Razavi & Myers; 2002: 71-73)*

2.1.6 Online Investment

With the advent and subsequent growth of computers along with the development of Internet facilities, online investment has become a much

practiced mode of investment. For a considerable period of time, online investment has come to replace physical investment practices.

The specialty of online investment is the fact that the quality of the services provided in this domain is top notch. The pace of transaction, as well as the fact that the investors might be able to carry on the trade themselves without the need of any external help has made online investment a lucrative proposition.

The online investment services allow the investors to invest their money in mutual funds and many other favorable investment options on a global basis. In this context, another important aspect is that the investors operating in the global market also prefer to invest in foreign stocks. The foreign direct investments that are made in outstation markets have also emerged as one of the preferred investment solutions for the global investors. The online investment brokers play a crucial role in the context of online investment as they are the ones who are normally entrusted with the responsibility of managing the affairs of the online investment market besides facilitating the transactions between the buyers and the sellers. *(Brealey, Razavi & Myers; 2002: 83)*

Over the years, the investment brokers operating online have been developing ways that help the customers to make deals in the online investment market with convenience and ease. The facilities that are available from different websites vary, but the general emphasis of all the websites is on providing top quality of service to their customers in order to satisfy them.

The online investment tools are also equally important as the online investment brokers. Over the years, these devices have been playing an important role in the context of online investments by enabling the clients to make various investment related calculations and find out the exact amount of return that would be received by them.

2.1.6.1 Online Investment Services

With the continuous development of the World Wide Web, online investment services have assumed a special role in the field of investment and related activities. The online investment service providers have been critical in making online investment a better choice than physical investment. The efficient use of different innovations in the field of communication technologies has made it possible for the providers to furnish their clients with viable online investment services that include the opportunity to trade in other countries, as well.

The mutual companies are the leading providers of online investment services in a lot of countries including the United States, where insurance firms and banks function as online investment service providers. These are normally managed by the members of the organization rather than the shareholders. If the mutual company happens to be a savings bank or a savings association, then the members are granted the status of depositors, and if the mutual company operates as an insurance company, then the members are regarded as policyholders. *(Fielding; 1999: 408)*

The role of online brokers is quite significant as far as online investment is concerned as they are responsible for looking after the transactions of their clients in the online investment market. However, it is advisable that the clients judge the credibility of the broker before signing the agreement with the broker. It is extremely important from the point of view of the investors that they sign a formal contract with the broker. This agreement ensures that the investor has certain rights by law and can exercise them as specified by the contract. The online financial planners are also important in that they are responsible for making a plan that suits the interests of their respective clients and helps them derive the maximum possible return from their investments. *(Fielding; 1999: 410-411)*

The investment clubs consist of groups of people who collect money from their own members for the purpose of investment. Decisions are normally taken after careful market analysis by the members. Such investment clubs make arrangements for meetings in order to popularize the concept of online investment services.

2.1.7 Return on Investment

Return on investment or ROI refers to how money can be received from investments. It is represented as a ratio of money earned or suffered as a loss in an investment in association to the invested amount of money. The money, which is earned, is known as profit, interest, net income or gain. The money lost is known as loss. The return on investment (ROI) is normally expressed as a percentage. *(Musiela & Rutkwoski; 1998: 101)*

The amount of money that is invested is termed as capital, asset or principal. Return can either be positive or negative, which means return can either mean a profit or loss. Return on investment can be calculated on previous or present investment and it is also applied for calculating the estimated rate of return of future investment. Return on investment (ROI) is frequently used on an annualized or yearly basis.

Return on investment is implemented for the comparison between the returns, which are expected to yield on investments, if the comparison cannot be performed conveniently with the help of monetary values. Return on investment is also known in a number of names, for example the rate of return (ROR), rate of profit or simply return. The ROI measures the ability of a particular company to utilize its assets for the purpose of generation of extra value for the shareholders. ROI is estimated as Net Profit/Net Worth. The return on investment can be improved in the following ways:

⌡ By decreasing expenses
⌡ By increasing profits

〕 By speeding growth *(Hull; 2002: 80)*

The different formulas for calculating the ROI are the following:

Return on investment is equal to gain from investment minus cost of investment divided by cost of investment. In this case, the cost of investment is deducted from the gain from investment and then it is divided by the cost of investment. The result is represented as a ratio or percentage.

ROI= Net Income/Book Value of Assets

Or, ROI= Net Income + Interest (1-Tax Rate)/Book Value of Assets

Return on investment or ROI is a highly popular measurement due to its convenience. The factors on which the ROI depends for its amplification are the following:

〕 The term of the project (the bigger, the more the increase)
〕 The rate of depreciation
〕 Capitalization policy
〕 The time lag between the disbursement of money and the recovery of money (the more the time lag, the more the increase)
〕 The rate of appreciation of investment

2.1.8 Investment Risk

On ground of assurance of the return, there are two kinds of Investments - Riskless and Risky. Riskless investments are guaranteed, but since the value of a guarantee is only as good as the guarantor, those backed by the full faith and confidence of a large stable government are the only ones considered riskless. Even in that case the risk of devaluation of the currency (inflation) is a form of risk appropriately called "inflation risk." Therefore no venture can be said to be by definition risk free - merely very close to it where the guarantor is a stable government.

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2.1.8.1 Types of Risk

Depending on the nature of the investment, the type of investment risk will vary.

a) Capital Risk

A concern with any investment is that you may lose the money you invest - your capital. This risk is therefore often referred to as capital risk. *(Demeterfi, Derman, Kamal & Zou; 1999: 10)*

b) Currency Risk

If the assets you invest in are held in another currency there is a risk that currency movements alone may affect the value. This is referred to as currency risk. *(Demeterfi, Derman, Kamal & Zou; 1999: 10)*

c) Liquidity Risk

Many forms of investment may not be readily saleable on the open market (e.g. commercial property) or the market has a small capacity and may therefore take time to sell. Assets that are easily sold are termed liquid; therefore this type of risk is termed liquidity risk. *(Demeterfi, Derman, Kamal & Zou; 1999: 11)*

d) Financial Risk

The risk that there may be a disruption in the internal financial affairs of the investment, thereby causing a loss of value, is called financial risk. A prime example of that form of risk was experienced by the investors in Enron, or one of the dot-com stocks that really never did have a profitable financial footing. Many of the employees of Enron experienced both liquidity and financial risk as the price decline in the stock of that company occurred just as there was a freeze on stock liquidation in their retirement plans. *(Demeterfi, Derman, Kamal & Zou; 1999: 11)*

e) Market Risk

Perhaps the most familiar but often least understood form of investment risk is market risk. In a highly liquid market like the collective stock exchanges in the United States and across the developed world, the price of securities is set by the forces of supply and demand. If there is a high demand for a given issue of stock, or a given bond, the price will rise as each purchaser is willing to pay more for the security than the last one. The reverse of that occurs when the sellers want to rid themselves of an issue more than the buyers want to buy it. Each seller is willing to receive less than the last one and the market price, or valuation, declines. *(Demeterfi, Derman, Kamal & Zou; 1999: 12)*

2.2 Review of NRB Directives

Nepal Rastra Bank is the central monitoring body of the financial institutions of Nepal. For the smooth and effective operations of FI, the bank provides circulars in regular time interval. The circular related to the investment are as follows;

a) Provision for Investment in Deprived Sector

Commercial banks are compulsorily required to extend their credit and investment in the deprived sector such as co-operative institutions and the rural banks that are licensed through NRB. The new provision obligates the commercial banks to invest 3.0 % of the total loan and advances to the deprived sector.

b) Provision for Investment in Productive Sector

Nepal, being a developing country needs to develop infrastructure and other primary productive sectors like agriculture, industry etc. For this, NRB has directed commercial banks to extend at least 40% of their credit to the productive sectors like agriculture sector and industrial sectors.

c) Investment in Stocks and Securities

Commercial banks are also required to minimize exposures to risk involved in investing the deposits of the saver and other financial resources at their disposal in earning assets. Commercial banks are required to compile and submit their financial reports keeping in view:

- Nepal Rasta Bank Act
- Commercial Bank Act
- International Accounting System
- Nature and type of their respective transaction
- Directives of the Nepal Rastra Bank
- Monetary and Financial Statistics Manual of IMF

d) Investment Management Regulation

A commercial bank formulating a written policy may decide to invest in shares and securities of an organized institution. However, such investment is restricted to 10% of paid up capital of the organization. However, the cumulative amount of such investment in all the companies in which the bank has financial interest shall be limited to 20% of the paid up capital of the bank. But the total amount of investment in share and securities of the organized institution is restricted to 30% of the paid up capital of the bank.

Likewise, Commercial Banks are not allowed to invest in any shares, securities, and hybrid investment issued by any banks and financial institutions licensed by NRB. Where such investment exists prior to issuances of this directive, such investment brought within the restrictive limitation by the FY 2003//04. However, investments on rural microfinance development banks' share are free from such restriction.

2.3 Review of Journals and Articles

Andrés and Rowland (2008), in their article, *Investment Flows into Emerging Markets,* have stated that investment flows constitute an important part of the

balance of payments, and it is of this reason crucial for policy makers to understand their behavior and determinants, both to be able to evaluate the impact of policy decisions on the balance of payments and to be able to correctly forecast this. Investment flows have, indeed, played an important role in recent emerging market crises, and large inflows of portfolio investment, in particular, often turns out to be a curse rather than a blessing, when such flows come to a sudden stop or even reverse.

Policy makers should play a major role in fostering good fundamentals as a result of sound, transparent and publicly known policies. Good fundamentals affect inflows as reflected in our empirical results. In addition, sound fundamentals can absorb sudden stops at a much lesser cost than unbalanced economies. Unexpected transitory shocks to the capital account of an unbalanced economy may translate into a permanent shock with high output costs. However, good fundamentals take time to consolidate, and their impact on capital flows might not be instantaneous. Finally, not everything is asymmetric information and sound fundamentals. As shown, the influence of external factors continues to be, and should continue to be a main determinant of capital inflows to developing countries as the global economy tends to greater integration. The above policy orientation does not solve the issue of volatile and scarce capital flows. However, it should be able to alleviate some of the threats posed in the current global capital markets with asymmetric information.

Giri (2008), in his article, *Managing Investment Portfolio,* has confronted with the problems of managing investment portfolio particularly in times of economics low down like ours. According to the study, a rational investor would like to diversify investment in different classes of assets to minimize risks and earn a reasonable rate of return. The study states that commercial banks have continuously been reducing interest rates on deposits. Many depositors are exposed to the increasing risk of non-refund of their deposits

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because of the mismanagement in some of the banks and financial institutions and accumulation of huge non-performing assets with them.

Few depositors of cooperative societies lost their deposits because some of the cooperatives were closed down because of their inability to refund public deposits. An investor in days of crisis has to make an effort to minimize the risk and at least earn a reasonable rate of return on his aggregate investment. An investment in equity share can earn dividend income as well as capital gain in the form of bonus share and right share until an investor holds it and capital profit when he sells it in the stock market. Making investment in fixed deposits with commercial banks is a normal practice among the common people. Normally fixed deposits with banks are considered risk-less, but they also are not hundred percent free of risk.

Naudé, Oostendorp and Serumaga-Zake (2009), in their article, *Determinants of Investment and Exports of South African Manufacturing Firms: Firm-Level Survey Results,* has utilized data from a firm-level survey of 61 manufacturing firms in South Africa to identify the determinants of investment and exports of manufacturing firms in South Africa. The sample was chosen to include a region of South Africa where manufacturing firms were particularly subject to adjustment shocks over the past six years. These were adjustment shocks relating to incorporation of so-called homeland areas into South Africa, and the greater liberalization of the South African economy. It was deemed necessary to identify the determinants of investment and exports in manufacturing as this sector is vital for growth and job creation, and need higher levels of investment than in the past as well as higher exports to be internationally competitive.

The implementation of tariff reform and tariff reductions, in accordance with the country's GATT obligations, reduced the level of protection from international competition that many South African firms enjoyed. During the

apartheid era, some manufacturing firms enjoyed "double" protection in that tax, labor and other incentives were awarded to manufacturing firms that were located in the so-called homeland areas. In order to analyze how these firms where adjusting to greater competition, their investment and export behavior, and the determinants thereof, was investigated. The survey results can be summarized as follows, with reference to the results from other African countries. Exporters are more efficient than non-exporters, and that exporting at any scale is only a real possibility for firms if they have achieved a sufficient level of efficiency. Thus, improving firm efficiency and overcoming labor cost disadvantages are serious firm level constraints facing South African manufacturing firms in their adjustment to globalization.

Brown, Florax and McNamara (2010), in their article, *Investment Flows in U.S. Manufacturing,* contribute to the relatively small literature on the regional investment. A conceptual model of location determinants is developed, which considers the importance of agglomeration economies, market structure, labor availability and productivity, infrastructure, and fiscal determinants. A cross-regressive model containing spatially lagged explanatory variables and a spatial Durbin model containing spatially lagged explanatory variables, including the lagged dependent variable, are estimated.

The study find a positive impact associated with local agglomeration economies, market size, labor productivity, and transportation infrastructure. Spatial spillovers are found to be of a competitive nature at the state level, implying that a factor that attracts more investment to a particular state is associated with lower investments in neighboring states. Market structure was found to be the most important factor in investment location, which suggests that the manufacturing sector as a whole still prefers to locate near demand centers. One potential policy implication is that policy makers should focus on economic development policies that attract people if they wish to attract manufacturing investment. Moreover, the attempts to increase the investment

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flows in a particular state may have competitive implications for investment flows to neighboring states. This may point to the possibility of unintended consequences on the impact of states' economic development policies as well as any federal transfers used to attract investment.

2.4 Review of Thesis

Basyal (2006), in her thesis, *A comparative Study on Investment Policy of Nepal Investment Bank Ltd. and Himalayan Bank Ltd.,* has the main objective to examine and evaluate the investment policy of Nepal Investment Bank and Himalayan Bank. The other specific objectives of the study are;

a. To compare the investment policy of concern banks and to discuss the fund mobilization of these two banks.

b. To evaluate the liquidity, assets management efficiency, profitability and risk position.

c. To determine the growth rate of bank in terms of deposit, loan and advances, investment and profitability of the banks.

The major findings of the study are;

a. The mean current ratio of both Banks is almost same. However, NIBL has more consistency than HBL in terms of current ratio. Likewise, the mean ratio of cash and bank balance to total deposit of NIBL is higher than that of HBL. It states that the liquidity position of NIBL is better than that of HBL.

b. The mean ratio of investment on government securities to current asset of NIBL is lower than that of HBL. It states that HBL uses to invest its current assets in government securities more than that of NIBL.

c. The mean ratio of total investment to total deposit ratio of NIBL is lower than that of HBL. It concludes that HBL has better utilization of deposits to investment than NIBL.

d. The mean ratio of investment on government securities to total working fund ratio of NIBL is lower than that of HBL. Similarly, the mean ratio

of investment on shares and debenture to total working fund ratio of NIBL is lower than that of HBL.

e. The total investment of both banks is in increasing trend where it will be Rs. 11701 millions in NIBL and Rs. 12784 millions in HBL in the fiscal year 2011/12.

f. There is highly positive relationship between net profit and outside assets of both NIBL and HBL.

Shah (2007), in his thesis *A Study on Investment Portfolio of Commercial Banks in Nepal*, has the main objective to identify the current situation of investment portfolio of CBs in Nepal. The other specific objectives are as follows:

a. To analyze the investment portfolio of Commercial Banks

b. To analyze the risk and return of selected commercial banks on investment using Portfolio concept.

c. To forecasting and examine the trend of investment and to provide complementary measures based on analysis.

The major findings of the study are;

a.   Proper investment on various securities i.e. balance allocation of funds on various government securities such as Treasury bills, National saving bonds, Development bonds etc and fixed income percentage rate that help to reduce the variability of return. In the analysis of risk and return comparatively SCBNL have more return from investment on government securities like same NABIL has better position on investment on loan and advances.

b.   The return on share and debenture of commercial banks shows wide fluctuation. These fluctuations in returns are caused mainly by the volatility of the shares prices in market and by the changes in dividends in some extent. Comparatively to other assets, share and

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debenture has higher return on higher risk. Hence, it is cleared from analysis that investment on share and debenture is highly risky assets.

c.   The return is slightly lower than average return from loan and advances and share and debentures. The portfolio risk on investment is less than that of risk on loan and advances and risk on share and debenture. It shows there is vital role of government securities to reduce the risk.

d.   The study shows that the portfolio return is decreasing trend every year. It shows the investment portfolio concept is not using properly by the selected banks.

e.   SCBNL is the bank that mobilizes its total deposits more effectively on government securities. EBL has concentrated to mobilize its depositor's funds in loan and advances. HBL, NSBIBL and NIBL are not so successful to mobilize its depositor's funds in government securities. But NSBIBL is also more successful to mobilize depositor's funds in loan and advances as well as share and debentures. And NIBL effectively mobilize its depositor's funds in share and debentures.

Satyal (2008), in her thesis, *A study on Portfolio Investment Analysis of Commercial Banks in Nepal*, has the main objective to analyze the portfolio investment of commercial banks. The other specific objectives are;

a. To examine the existing situation of portfolio investment management of Nepalese commercial bank.

b. To analyze risk and return of commercial banks.

c. To analyze the investment and loans and advance portfolio of commercial banks.

d. To show the present position trend of loan and advance and investment to total deposit and forecast it.

The major findings of the study are;

a. The industrial mean ratio of investment to total deposit is 21.86%. The only EBL has a greater ratio above industrial mean ratio i.e. 24.77>21.8. But other banks have lower investment to total deposit ratio than industrial mean ratio. It shows that EBL has effective mobilization its deposit on investment to generate the return.

b. Among four commercial banks HBL has invested its more funds on government securities (i.e. risk free assets) and lesser fund on share and debenture (i.e. risky assets). All banks have invested more than 83% amount in government securities. Only BOKL has invested it's 0.63% on non-resident sector. None of the banks have invested any amount on NRB bond.

c. All of the selected commercial banks are granting very high amount its loan and advances to private sector. NIBL and HBL have given second priority to government enterprise and EBL and BOKL give second priority to foreign bills purchase and discount.

d. BOKL stock has the highest expected return i.e. 8.34% and HBL has lowest expected return i.e. -8.82%. NIBL has also negative return i.e. -7.71%. The market expected return is -6.47%. The risk of BOKL is the highest i.e. 57.14% and HBL has 36.03% respectively. The market risk is 15.68%.

e. HBL has the highest portfolio return i.e. 4.85%, NBIL stock has lowest (i.e. negative -1.19%) portfolio return and it has the highest portfolio risk i.e. 8.46%. It means NIBL invest its amount in risky assets so it become in loss. EBL and BOKL have a portfolio return of 4.79% and 4.80% respectively and portfolio risk is 0.28% and 5.77% respectively.

Gautam (2009), in her thesis, *Investment Portfolio Analysis of Joint Venture Banks*, has the main objective to identify the current situation of investment portfolio of joint venture banks in Nepal. The specific objectives are as follows;

a. To analyze the risk and return ratios of commercial banks.

b. To evaluate the financial performance of joint venture banks.

c. To study exiting investment policies taken by JVBs in various sectors.

d. To study portfolio structure of JVBs in investment as compared to other joint venture banks.

e. Preference given by JVBs for investment between loan investment, investment in real fixed assets, investment in financial assets.

The major findings of the study are;

a. SCBNL and HBL have better position. NBBL and NABIL have a low position in the industry. But EBL has a very low position in the industry because of having lowest mean return on shareholder's fund.

b. SCBNL has the highest mean return and EBL has the lowest return. Expect EBL, all other four banks i.e. NABIL, SCBNL, HBL and NBBL have good performance.

c. Among other joint venture banks, SCBNL has the highest return and EBL has above mean return than industry average. SCBNL and EBL mobilizes the funds in investment title is higher than the standard ratio.

d. NABIL, SCBNL and HBL are investing low amount of deposits on loans and advance which is lower than industry average and NBBL and EBL have invested a high amount of deposits to loans and advances title which is higher than industry average.

e. NABIL is investing the highest amount of funds on NRB bond as compared to other JVBs i.e. 3%. NBBL has invested no amount of funds in this title and EBL has invested the lowest of funds i.e 0.4 % and SCBNL and HBL have invested above industry average.

Tamrakar (2010), in his thesis, *Investment Analysis of Nepalese Banks*, has the main objective to analyze the trend of investments in private sectors. The other specific objectives of the study are;

a. To analyze the trend of repayment in private sectors for 10 years.

b. To measure the effectiveness of the program in terms of the investment and repayment in rural and urban sector.

c. To evaluate the banking procedures and services in disbursing loan in this sector.

The major findings of the study are;

a. The target of 12% investment of total outstanding liabilities in priority sector and 3% out of which has been invested in deprived sector has been met by RBB.

b. Trend analysis of 10 years shows the increasing trend of investment in priority sectors which shows that the CBs are giving due consideration to increase investment in priority sector.

c. Interest charged on the loan disbursed in this sector is fairly less than the interest charge on loans for other purposes. In addition to this, there is high overhead cost incurred for supervision, administration and others in this program.

d. Regression analysis shows positive relation between investment and repayment. The Chi square test of effectiveness of program is more effective in rural and semi rural area as compared to the urban areas. Investment on agriculture is higher than investment on industry and service sector.

e. The study revealed that the procedure of loan disbursing itself is complicated for the borrowers to understanding. In fact, if the supervisors make the scheduled supervision & inspection & the frequent contact with the borrowers, the chance of misuse of the loan can be minimized.

Sharma (2010), in his thesis, *Investment Analysis of Commercial Banks, A Comparative Study on HBL and Nepal SBI,* has the main objective of the study is to evaluate the investment policy of HBL and SBI. The other specific objectives of the study are;

a. To measure the liquidity, assets management, efficiency, profitability and risk position of Himalayan Bank in comparison to that of Nepal SBI.

b. To study the relationship between investment and deposits of the banks.

c. To analyze investment trend, deposits trend and total income and their projection for next five years.

The major findings of the study are;

a. HBL has good deposits collection and has made enough investment on government securities but maintained low investment policy than that of Nepal SBI.

b. Both the banks should maintain required current ratio, as the current ratio of both banks is not sufficient. They have to consider more on the liquidity of the deposits as they are for the sake of the bank's reputation.

c. As banks have invested less on shares of other companies so recommended to mobilize its fund for business and industries for industrial support.

d. As ratio of interest income to total income is too high in both banks thus its income should not be limited to interest earned from loan.

2.5 Research Gap

All of the previous studies made are concerned with comparing the total investment with the total flow of loan and advances, and do not enlightens on each component of the investment. Tracing this defect, the present study is conducted to analyze the investment priority given by the banks in each component of the investment, such as treasury bond, development bonds, corporate securities and debentures, interbank lending and so on. Further, the study also analyzes the primary data to understand the views of bank-related personalities, mainly employees and investors.

CHAPTER – III
RESEARCH METHODOLOGY

3.1 Research Design

Research design is the plan, structure and strategy of investigation conceived so as to obtain answer to research questions and to control variance. It is arrangement for collection and analysis of data. To achieve the objective of this study, descriptive and analytical research design has been used. Some financial and statistical tools have been applied to examine facts and descriptive techniques have been adopted to analyze the investment policy of commercial banks.

3.2 Population and Sample

Currently there are 31 commercial banks operating in Nepal. The study of all these banks in this study is almost impossible. So, 2 commercial banks, namely Everest Bank Limited and Nepal Investment Bank Limited, have been selected randomly as sample of the study.

3.3 Nature and Sources of Data

The study is based on secondary data and primary data. The secondary data have been extracted from the annual reports of EBL and NIBL. Besides annual reports, the official website of sampled banks, NEPSE, SEBON and NRB have also been reviewed. While the primary data have been collected through conduction questionnaire, targeting to the employees of the banks and investors of shares as the respondents.

3.4 Data Analysis Tools

The collected data have no meaning if such data are not analyzed. To analyze the data in this research, the researcher has used some statistical and financial tools which are explained here.

3.4.1 Financial Tools

The major financial tools used in this research are as follows;

A) Total Net Investment to Total Assets

Investment is the one of the sources of income of bank. The bank earns interest income from government securities, bond and other investment, and dividend & capital gain from corporate shares. The net investment to total assets measures what portion of the total fund available has been mobilized on investment excluding provision.

$$\text{Total Net Investment to Total Assets} = = \frac{\text{Total Net Investment}}{\text{Total Assets}}$$

B) Investment in Government Securities to Total Investment

Government securities are the fixed income securities issued by governments. These securities are among the safest of all investment, as the government is unlikely to default on interest or on principal repayments. As a result, the government securities has enticed the bank for investment. The investment in government securities to total investment measures what portion of the total investment is occupied by government securities.

$$\text{IOGS to TI} = \frac{\text{Inv. on Tresury Bill} + \text{Inv. on Development Bonds} + \text{Investment on Savings Bonds.}}{\text{Total Investment}}$$

C) Investment in Corporate Shares and Debentures to Total Investment

This ratio shows that the banks' investment on shares and debentures of other companies. It can be calculated by dividing investment on share and debenture by total investment.

$$\text{Investment on Shr. \& Deb. to Total Inv.} = \frac{\text{Investment on Shr. \& Deb.}}{\text{Total Investment}}$$

D) Investment in Inter Bank Lending to Total Investment

Banks are required to hold an adequate amount of liquid assets, such as cash,

to manage any potential withdrawals from clients. If a bank cannot meet these liquidity requirements, it will need to borrow money in the interbank market to cover the shortfall. Some banks, on the other hand, have excess liquid assets above and beyond the liquidity requirements. These banks will lend money in the interbank market, receiving interest on the assets. Thus, the interbank lending to total investment clarifies the role of interbank lending on total investment.

$$IOIBL = \frac{Investment\ on\ Inter\ Bank\ Lending}{Total\ Investment}$$

E) Return on Government Securities

The return on government securities is computed by dividing interest income on government securities by total investment on government securities, which can be presented as:

$$ROGS = \frac{Interest\ Income\ on\ Gov. Securities}{Total\ Investment\ on\ Gov. Securities}$$

F) Return on Corporate Share and Debentures

The return on Shares and Debentures considers dividend yield, capital gain yield i.e. change in market price, and the interest on debenture. The dividend yield is only a partial indication of the return; hence, the return on Share and Debenture significantly depends on the change in its Share Price.

$$ROCSD = \frac{P_{t+1} - P_t + D_{t+1}}{P_t} + \frac{Interest\ on\ Debenture}{Inv.on\ Debenture}$$

G) Return on Inter Bank Lending

The bank earns interest on interbank lending. The return on interbank lending indicates how much interest income it has collected from both local licensed institutions lending and foreign bank lending. Higher the ratio is considered favorable.

$$ROIBL = \frac{Interest\ from\ Local\ Licensed\ Institution + Interest\ from\ Forlegn\ Banks}{Total\ Investment\ in\ Inter\ Bank\ Lending}$$

H) Provision on Investment

Investment in corporate shares and debenture is one of the sources of income to bank. However, the market situation does always remain favorable, and thus the market price of the invested share can be lower than the par value. To confront which such situation, the bank keeps the provision on investment. Thus the provision on investment measures what portion of the investment has been kept as provision.

$$\text{Prov. on Investment} = \frac{\text{Provision for Possible Loss}}{\text{Total Investment}}$$

3.4.2 Statistical Tools

To achieve the objectives of the study set out in first chapter, the following statistical tools have been efficiently utilized in fourth chapter to analyze the data.

A) Mean

The arithmetic <u>mean</u> (or simply the mean) of a list of numbers is the sum of the list divided by the number of items in the list. The mean is the most commonly-used type of <u>average</u> and is often referred to simply as the average.

$$\text{Mean}(\bar{X}) = \frac{x_1 + x_2 + \ldots\ldots\ldots\ldots + x_n}{N}$$

B) Standard Deviation

Standard deviation is a widely used measure of the variability or <u>dispersion</u>, being algebraically more tractable though practically less <u>robust</u> than the <u>expected deviation</u> or <u>average absolute deviation</u>. It may be thought of as the average difference of the scores from the mean of distribution, how far they are away from the mean. A low standard deviation indicates that the data points tend to be very close to the <u>mean</u>, whereas high standard deviation indicates that the data are spread out over a large range of values.

$$\text{Standard Deviation } (\sigma) = \sqrt{\frac{\Sigma(X - \bar{X})^2}{N}}$$

C) Coefficient of Variation

The coefficient of variation represents the ratio of the standard deviation to the mean, and it is a useful statistic for comparing the degree of variation from one data series to another, even if the means are drastically different from each other.

$$\text{C.V.} = \frac{\text{Standard Deviation} \times 100}{\text{Mean}}$$

D) Correlation Coefficient

Two variables are said to have correlation, when they are so related that the change in the value of one variable is accompanies by the change in the value of the other. One of the widely used mathematical methods of calculating the correlation coefficient between two variables is Karl Pearson's correlation coefficient (r), which is defined by;

$$r = \frac{\Sigma(X - \bar{X})(Y - \bar{Y})}{\sqrt{(X - \bar{X})^2}\sqrt{(Y - \bar{Y})^2}}$$

E) Regression

Regression refers to any approach to modeling the relationship between one or more variables denoted Y and one or more variables denoted X, such that the model depends linearly on the unknown <u>parameters</u> to be <u>estimated</u> from the <u>data</u>. The simple regression line of Y on X is given by;

$$Y = a + bX \text{ .... (i)}$$

Where, Y = Dependent Variable

a = Constant

b = Regression Coefficient

X = Independent Variable

F) Probable Error

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

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

Where, r = the value of correlation coefficient

n = number of pairs of observations

if r < P.E., it is insignificant, i.e. there is no evidence of correlation

if r > 6 P.E., it is significant.

G) Trend Analysis

Trend analysis is an analysis of financial ratio over time used to determine the improvement of deterioration of financial situation. Using the least square method, the projection for two years is done. For the estimation of linear trend line, following formula has been used.

$$Y = a + bx$$

Where,

Y = dependent variable

a = y-intercept

b = slope of the trend line

x = independent variable

CHAPTER – IV

DATA PRESENTATION AND ANALYSIS

4.1 Secondary Data Analysis

Under this section, the data related to the investment of banks in each sector, i.e. in government securities, corporate shares and debentures, interbank, lending are analyzed with respect to the total investment and the return on such investment is evaluated.

4.1.1 Total Net Investment to Total Assets

Investment is the one of the prominent sources of income in bank. The interest and the dividend income achieved from investment buttresses the net profit of the bank. However, it seems that the bank has been less enticed in investment in comparison to granting loan and advances. To measure the preponderance of the total net investment on the total fund mobilized, the ratio of net investment to total assets of EBL and NIBL have been evaluated.

Table 4.1

Total Net Investment to Total Assets

FY	EBL			NIBL		
	TNI	TA	Ratio	TNI	TA	Ratio
2005/06	4200.52	15959.29	26.32	5602.87	21330.14	26.27
2006/07	4984.31	21432.57	23.26	6505.68	27590.84	23.58
2007/08	5059.56	27149.35	18.64	6874.03	38873.31	17.68
2008/09	5948.48	36916.83	16.11	7399.81	53010.80	13.96
2009/10	5008.31	41382.76	12.10	8635.53	57305.41	15.07
Mean			**19.29**			**19.31**
S.D.			**5.05**			**4.81**
C.V.%			**26.17**			**24.93**

(Source: Appendix-I)

The table manifests that the total net investment of the bank out of the total fund mobilization is comparatively lower, which indicates that the bank has given predilection to the loan and advances while mobilizing the available fund. Nonetheless, both the banks have put their effort to increase the investment amount in most of the fiscal years. As a result the net investment of EBL has increased from Rs. 4200.52 millions in the fiscal year 2005/06 to Rs. 5948.48 millions in the fiscal year 2008/09, and in the fiscal year 2009/10 it is Rs. 5008.31 millions, while the net investment of NIBL has ranged from Rs. 5602.87 millions in the fiscal year 2005/06 to Rs. 8635.53 millions in the fiscal year 2009/10. In addition, the total assets of the both the banks have undoubtedly increased in each fiscal year.

The table reveals that the total net investment to total assets of EBL has decreased during the entire periods, which means that the total net investment of the bank could not meet the same pace of growth that the total assets has followed. Consequently, the ratio of total net investment to total assets of EBL is 26.32% in the fiscal year 2005/06, which has decreased to 23.26% in the fiscal year 2006/07, then it has decreased to 18.64% in the fiscal year 2007/08, 16.11% in the fiscal year 2008/09, and finally it has decreased to 12.10% in the fiscal year 2009/10. In average, the bank has mobilized 19.29% of the total funds in the investment such as government securities, foreign securities inter - bank lending, and corporate shares and debentures. Also the fluctuation on the ratio is 26.17%, indicating lower variation.

Alike in EBL, the ratio of net investment to total assets of NIBL has followed decreasing trend up to the fiscal year 2008/09, indicating lower growth rate in investment than in total assets. The ratio is 26.27% in the fiscal year 2005/06, and 13.96% in the fiscal year 2008/09, and by the end of the fiscal year 2009/10, it has gradually increased to 15.07%. This decreasing phenomenon has signaled that the bank has been fascinated in other sectors in the quest of augmenting profit, and thus investment in government securities, corporate

shares and debentures, foreign and local licensed institutions etc. have been given low preference. In average, 19.31% of the total funds have been mobilized in investment and the variation in the ratio is 24.93%. On the basis of the average ratios, it can be considered that NIBL has mobilized the total funds in investment in subtle greater extent than EBL has done.

Figure 4.1

Total Net Investment to Total Assets
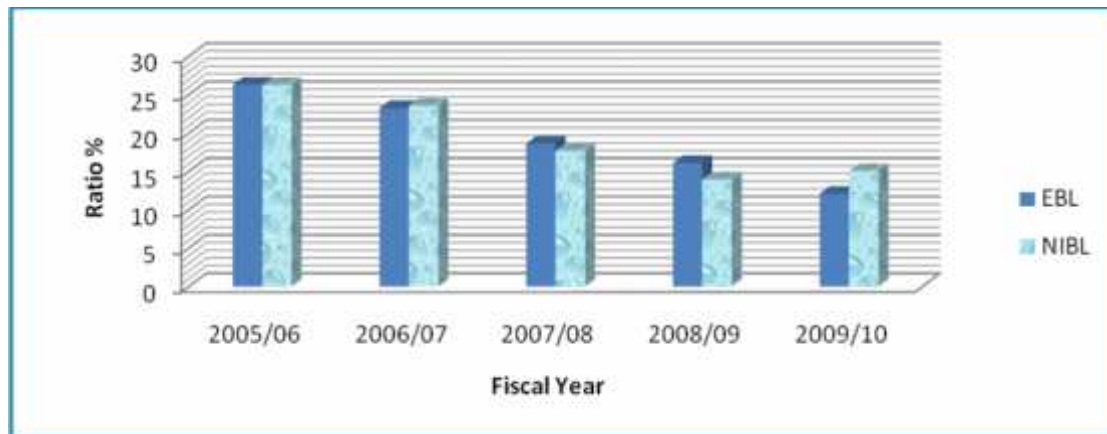
4.1.2 Investment in Government Securities to Total Investment

The commercial banks of Nepal seem to be highly enticed by the government securities while making investment, and thus the investment of the banks is highly dominated by the government securities, which involves treasury bill and development bonds. The investment in government securities to total investment delineates to what extent the investment of the bank is dominated by government securities.

Table 4.2

Investment in Government Securities to Total Investment

FY	EBL					NIBL				
	TB	DB	GS	TI	Ratio	TB	SB	GS	TI	Ratio
2005/06	3322.44	226.17	3548.61	4201.32	84.46	2522.30	0	2522.30	5602.87	45.02
2006/07	3614.54	1090.09	4704.63	4985.12	94.37	3256.40	0	3256.40	6505.68	50.05
2007/08	3237.98	1583.63	4821.61	5061.16	95.27	3155.00	0	3155.00	6879.42	45.86
2008/09	3371.43	1774.62	5146.05	5950.08	86.49	2531.30	0	2531.30	7403.11	34.19
2009/10	2745.28	1609.08	4354.36	5009.91	86.91	3911.85	290.00	4201.85	8638.83	48.64
Mean					**89.50**					**44.75**
S.D.					**4.43**					**5.59**
C.V.%					**4.95**					**12.48**

(Source: Appendix-I)

EBL has ignored savings bonds of the government securities and focused on treasury bills and development bonds. However, there is addition in development bonds by EBL, as a result the investment amount in development bonds has been increased in each fiscal year. In contrast, NIBL has ignored both development bonds and saving bond up to the fiscal year 2008/09, and in the fiscal year there is an investment of Rs. 290.00 millions in the saving bonds by NIBL. In contrast, the investment of EBL in treasury bills has fluctuated in the observed years, and thus it has ranged from Rs. 2745.28 millions in the fiscal year 2009/10 to Rs. 3614.54 millions in the fiscal year 2006/07. However, the investment of NIBL in treasury bills has increased in the fiscal year 2006/07, i.e. to Rs. 2072.38 millions in the fiscal year 2006/07 from Rs. 1559.51 millions in the fiscal year 2005/06, and then decreased in the remaining years, and finally the treasury bill has been decreased to Rs. 907.25 millions.

In overall, EBL has increased the total investment in government securities in most of the fiscal years, as a result the government securities of the bank has ranged from Rs. 4201.32 millions in the fiscal year 2005/06 to Rs. 5950.08 millions in the fiscal year 2008/09, and by the end of the fiscal year, it is Rs. 5009.91 millions. Also, the total investment in government securities of NIBL

has increased during the five consecutive fiscal years, and thus it has ranged from Rs. 5602.87 millions in the fiscal year 2005/06 to Rs. 8638.83 millions in the fiscal year 2009/10.

Moreover, the investment in government securities to total investment of EBL has fluctuated during the periods, and thus it has ranged from 84.46% in the fiscal year 2005/06 to 95.27% in the fiscal year 2007/08, while in the fiscal year 2009/10 the ratio is 86.91%. In average, the government securities have covered 89.50% of the total investment and the variation in such coverage is 4.95%. Similarly, the investment in government securities to total investment of NIBL has fluctuated in each fiscal year, and thus it has ranged from 34.19% in the fiscal year 2007/08 to 50.05% in the fiscal year 2006/07. In average, the government securities have occupied 44.75% of the total investment with 12.48% variation.

Finally, it has been ascertained that the banks are more enticed toward the treasury bill than the development bond and saving bonds. Although the coverage of government securities in total investment has fluctuated in the observed periods, the government securities still have greater preponderance in total investment than other form of investment. On the basis of average ratio, it can be avowed that EBL has focused more on government securities than NIBL.

Figure 4.2

Investment in Government Securities to Total Investment
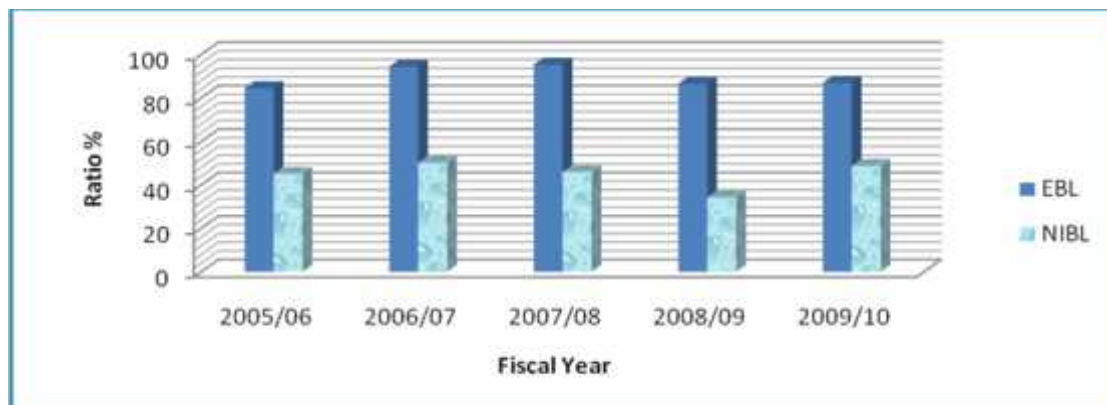
4.1.3 Investment in Corporate Shares and Debentures to Total Investment

Corporate shares and debentures is another field where the bank is interested to make investment. The investment in corporate shares and debenture to total investment depicts the weight of corporate share and debentures.

Table 4.3

Investment in Corporate Shares and Debentures to Total Investment

FY	EBL					NIBL				
	Shr.	Deb.	CSD	TI	Ratio	Shr.	Deb.	CSD	TI	Ratio
2005/06	19.89	0.00	19.89	4201.32	0.47	17.74	0	17.74	5602.87	0.32
2006/07	19.89	0.00	19.89	4985.12	0.40	35.25	0	35.25	6505.68	0.54
2007/08	16.23	84.93	101.15	5061.16	2.00	59.95	0	59.95	6879.42	0.87
2008/09	17.11	84.93	102.04	5950.08	1.71	64.27	0	64.27	7403.11	0.87
2009/10	17.11	84.93	102.04	5009.91	2.04	66.65	0	66.65	8638.83	0.77
Mean					**1.32**					**0.67**
S.D.					**0.73**					**0.22**
C.V.%					**55.43**					**31.92**

(Source: Appendix-I & II)

EBL has shown no interest in corporate debenture and bond for investment up to the fiscal year 2006/07, and thus it has focused only in corporate shares in such periods; limited to the share of five companies, and from the fiscal year 2007/08, the bank has invested in the debenture issued by the Nepal Electricity Authority, whereas NIBL has invested only in corporate shares.

Moreover, the corporate investment of EBL has remained precisely Rs. 19.89 millions, in the two fiscal years of the beginning periods, Rs. 101.15 millions in the fiscal year 2007/08, and Rs. 102.04 millions in the fiscal year 2008/09 and 2009/10. Consequently, the corporate share and debenture investment to total investment of the bank has fluctuated during the observed periods and thus it has ranged from 0.40% in the fiscal year 2006/07 to 2.04% in the fiscal year 2009/10. In average, the corporate investment of EBL has represented miniature share of total investment, i.e. just 1.32%, which has varied by 55.43%.

Similarly, the corporate share investment of NIBL has increased in the last five fiscal years, i.e. from Rs. 17.74 millions in the fiscal year 2005/06 to Rs. 66.65 millions in the fiscal year 2009/10. Eventually, the representation of corporate investment of NIBL in total investment has fluctuated during the observed periods and thus the ratio has ranged from 0.32% in the fiscal year 2005/06 to 0.87% in the fiscal year 2007/08 and 2008/09, however, in the fiscal year 2009/10, it is 0.77%. In average, the representation of corporate investment in total investment of the bank is 0.67% with the variation of 31.92%.

Comparing the banks, it can be inferred that NIBL has given less preference to corporate share and debenture investment than EBL, as a result the preponderance of corporate share and debenture on total investment in NIBL is lower than that in EBL.

Figure 4.3

Investment in Corporate Shares and Debentures to Total Investment
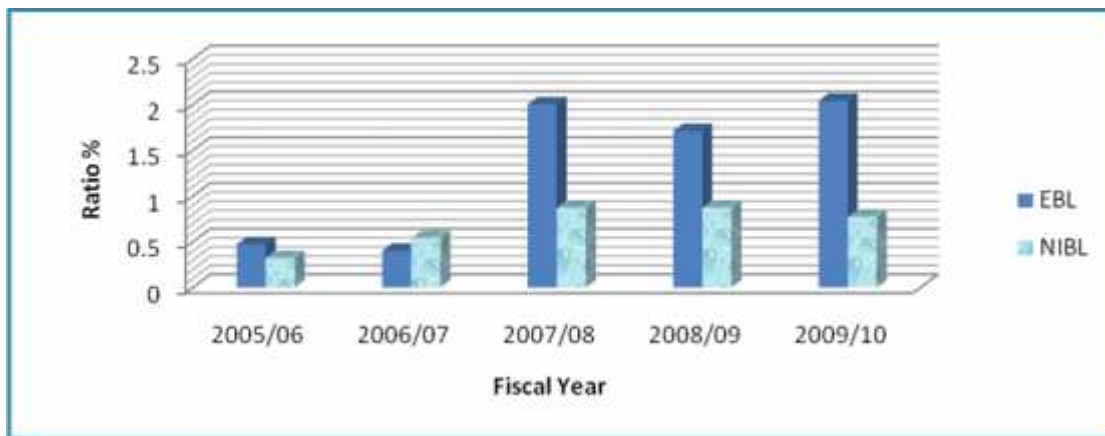
4.1.4 Investment in Inter Bank Lending to Total Investment

Interbank lending involves lending to both local licensed institutions and foreign banks for a short period of time, which in turn returns interest, and thus is the other sector of bank for investment. The ratio of investment in interbank lending to total investment measures the relationship between them.

Table 4.4

Investment in Inter Bank Lending to Total Investment

FY	EBL					NIBL				
	Local	Foreign	IBL	TI	Ratio	Local	Foreign	IBL	TI	Ratio
2005/06	0	632.82	632.82	4201.32	15.06	19.71	3043.12	3062.83	5602.87	54.67
2006/07	0	260.60	260.60	4985.12	5.23	19.64	3194.39	3214.03	6505.68	49.40
2007/08	0	138.40	138.40	5061.16	2.73	0	3664.48	3664.48	6879.42	53.27
2008/09	0	702.00	702.00	5950.08	11.80	0	4807.54	4807.54	7403.11	64.94
2009/10	261.80	291.72	553.52	5009.91	11.05	370.00	4000.33	4370.33	8638.83	50.59
Mean					**9.17**					**54.57**
S.D.					**4.52**					**5.51**
C.V.%					**49.26**					**10.10**

(Source: Appendix-I)

The table depicts that EBL has practiced interbank lending with both the local licensed institutions and foreign banks only in the fiscal year 2009/10. Generally, the foreign bank lending has ranged from Rs. 138.40 millions in the fiscal year 2007/08 to Rs. 702.00 millions in the fiscal year 2008/09. In overall as well, the total interbank lending of EBL is same to the foreign lending up to the fiscal year 2008/09, since the bank has neglected local lending. Moreover, the total interbank lending to total investment has decreased in the last four fiscal years, and thus the ratio is highest, 2.73%, in the fiscal year 2007/08 and lowest, 15.06%, in the fiscal year 2005/06. In average, the total interbank lending has represented 9.17% of the total investment with 49.26% variation.

Likewise, NIBL has ignored interbank lending to local licensed institutions for in the fiscal year 2007/08 and 2008/09. However, the bank has shown interest in foreign interbank lending and thus the bank has invested in foreign bank in each fiscal year. Also, the foreign interbank lending of NIBL has ranged from Rs. 3043.12 millions in the fiscal year 2005/06 to Rs. 4807.54 millions in the fiscal year 2008/09. Since the local interbank lending for the fiscal year 2007/08 and 2008/09 is nil, the total interbank lending in these periods is same as the foreign interbank lending and at the end of the fiscal year 2009/10 the

total interbank lending is Rs. 4370.33 millions. Nonetheless the interbank lending to total investment of NIBL has fluctuated during the periods, and thus the ratio has ranged from 49.40% in the fiscal year 2006/07 to 64.94% in the fiscal year 2009/10, with the variation of 10.10%.

Finally, it can be stated that the preponderance of interbank lending on total investment varies greatly in average in the observed banks. It has been observed that EBL has preferred government securities and NIBL has preferred interbank lending while making investment.

Figure 4.4

Investment in Inter Bank Lending to Total Investment
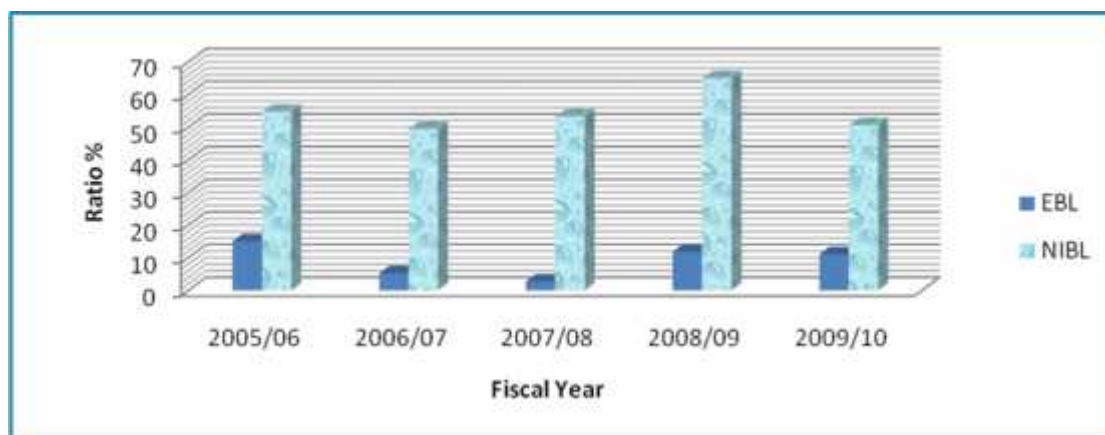
4.1.5 Return on Government Securities

The bank receives interest income on both the treasury bill and development bonds. The return on government securities measures what percentage of the total investment on government securities has been received as return in the form of interest income.

Table 4.5

Return on Government Securities

| FY	EBL					NIBL				
	Int.TB	Int. DB	IGS	GS	ROGS	Int.TB	Int. SB	IGS	GS	ROGS
2005/06	84.48	12.79	97.27	3548.61	2.74	82.42	0	82.42	2522.30	3.27
2006/07	114.35	14.21	128.56	4704.63	2.73	78.49	0	78.49	3256.40	2.41
2007/08	114.81	65.41	180.22	4821.61	3.74	99.99	0	99.99	3155.00	3.17
2008/09	205.44	84.32	289.76	5146.05	5.63	140.70	0	140.70	2531.30	5.56
2009/10	144.20	94.79	238.99	4354.36	5.49	167.87	1.75	169.62	4201.85	4.04
Mean					**4.07**					**3.69**
S.D.					**1.27**					**1.07**
C.V.%					**31.33**					**28.94**

(Source: Appendix-III)

The interest income on the treasury bills of EBL fluctuated during the periods, and such earning has ranged from Rs. 84.48 millions in the fiscal year 2005/06 to Rs. 205.44 millions in the fiscal year 2008/09. However, the interest income on the development bonds of the bank has followed increasing trend, and the thus the interest income of the bank has increased from Rs. 12.79 millions in the fiscal year 2005/06 to Rs. 94.79 millions in the fiscal year 2009/10. In total, the interest earning on government securities of the bank is Rs. 97.27 millions, Rs. 128.56 millions, Rs. 180.22 millions, Rs. 289.76 millions and Rs. 238.99 millions the fiscal year 2005/06, 2006/07, 2007/08, 2008/09 and 2009/10 respectively. Such interest earning has represented 2.74%, 2.73%, 3.74%, 5.63% and 5.49% return on government securities in the same fiscal year. In average, the return on government securities is 4.07% with the variation of 31.33%.

In most of the fiscal years, the interest earning of NIBL in Treasury bill has increased in most of the fiscal years. The interest earning on treasury bill has ranged from Rs. 78.49 millions in the fiscal year 2006/07 to Rs. 167.87 millions in the fiscal year 2009/10 and the interest earning in saving bond is Rs. 1.67 millions in the fiscal year 2009/10. In total the interest earning on

government securities of the bank is lowest, Rs. 78.49 millions, in the fiscal year 2006/07, and highest, Rs. 169.62 millions, in the fiscal year 2009/10. Such interest earning has shown 3.27%, 2.41%, 3.17%, 5.56% and 4.04% return on investment in government securities in the fiscal year 2005/06, 2006/07, 2007/08, 2008/09 and 2009/10 respectively. In average, the return on government securities is 3.69% with 28.94% variation.

Since the ratio of government securities to total investment of EBL is greater than that of NIBL, the return on government securities is also higher in EBL in comparison to that in NIBL. This might be due to policy of NIBL in making no investment in the development bonds in the entire periods and late investment in saving bonds, while in contrast EBL has adopted the policy of increasing the amount of development bonds.

Figure 4.5

Return on Government Securities
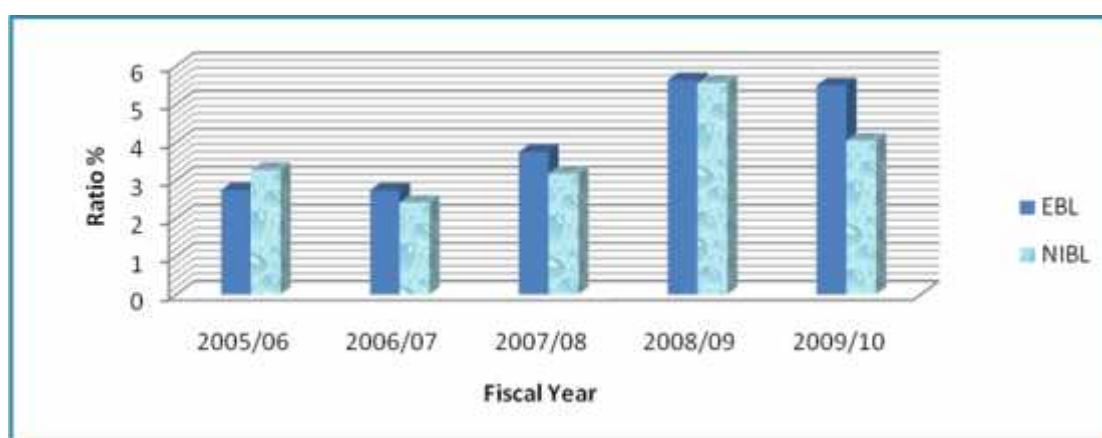
4.1.6 Return on Corporate Shares and Debentures

Corporate shares yield return in the form of dividend and capital gain, while debentures yield return in the form of interest. To measure the earning of the banks in the corporate share and debentures investment, the return on corporate shares and debentures has been evaluated.

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Table 4.6

Return on Corporate Shares and Debentures

FY	Corporate Shares			Debentures	Income	Inv. on	Return
	Div.	Price Change	Inc. on CS	Interest	on CSD	CSD	(ROCSD)
EBL							
2005/06	0.16	-0.80	-0.64	0	-0.64	19.89	-3.22
2006/07	0.25	1.48	1.73	0	1.73	19.89	8.70
2007/08	0.75	-1.60	-0.85	0	-0.85	101.15	-0.84
2008/09	0.00	0.50	0.50	6.57	7.07	102.04	6.93
2009/10	1.51	0.00	1.51	6.59	8.10	102.04	7.94
Mean							**3.90**
S.D.							**4.93**
C.V.%							**126.42**
NIBL							
2005/06	0.24	0	0.24	0	0.24	17.74	1.35
2006/07	0.21	0	0.21	0	0.21	35.25	0.60
2007/08	0.83	30.62	31.45	0	31.45	59.95	52.46
2008/09	1.61	-22.38	-20.77	0	-20.77	64.27	-32.32
2009/10	4.33	38.87	43.20	0	43.20	66.65	64.82
Mean							**17.38**
S.D.							**36.03**
C.V.%							**207.26**

(Source: Appendix-III)

The investment of EBL in corporate shares is quite melancholy, as the bank has experienced capital loss in the fiscal year 2005/06 and 2007/08. The capital loss in the fiscal year 2005/06 is due to the decrease in market price of Himalayan Distillery Limited and the capital loss in the fiscal year 2007/08 is caused by the decrease in the market price per share of Taragaon Regency Hotel. However, in other fiscal years, the bank has enjoyed a capital gain, and such gain has ranged from Rs. 0.50 millions in the fiscal year 2008/09 to Rs. 1.73 millions in the fiscal year 2006/07. Also, the bank has earned interest income of Rs. 6.57 millions in the fiscal year 2008/09 and Rs. 6.59 millions in the fiscal year 2009/10. Moreover, the return on corporate share and debenture of EBL has ranged from -3.22% in the fiscal year to 8.70% in the fiscal year 2006/07, and by the end of the fiscal year, the ratio is 7.94%. Thus, it can be said that the return on corporate shares and debentures of the bank is not irregular. Nonetheless, the bank has received 3.90% of the corporate shares and

debentures as return, which has varied by 126.42%, showing extremely inconsistent.

In contrast to EBL, NIBL has experienced no capital gain or capital loss in the first two fiscal years. In the remaining three fiscal years, the bank has experienced capital gains in two fiscal years, and capital loss in one fiscal year. More specifically, the capital gain is Rs. 30.62 millions in the fiscal year 2007/08 and Rs. 38.87 millions in the fiscal year 2009/10, while capital loss is Rs. 22.38 millions in the fiscal year 2008/09. Also the bank has received dividend on corporate share investment in each fiscal year, and thus the dividend income has ranged from Rs. 0.21 millions in the fiscal year 2006/07 to Rs. 4.33 millions in the fiscal year 2009/10. Though the bank has invested in corporate shares of eight local licensed institutions within these observed periods, the bank has bared capital gain or loss only in four licensed institutions. Summing the dividend, and capital gain, it has been revealed that the income on corporate shares and debentures has fluctuated during the periods, and thus it has ranged from Rs. -20.77 millions in the fiscal year 2008/09 to Rs. 43.20 millions in the fiscal year 2009/10. Moreover the return on corporate shares and debentures of the bank has fluctuated during the periods and thus it has ranged from -32.32% in the fiscal year 2008/09 to 64.82% in the fiscal year 2009/10. In average, the bank has received a return of 17.38% from total investment in corporate shares and debentures with 207.26% variation.

Comparing the banks it can be said that although the average return of NIBL is greater than that of EBL, the investment in corporate shares and debentures of NIBL is more risky than that of EBL, as the coefficient of variation in such return is higher in NIBL than in EBL.

Figure 4.6

Return on Corporate Shares and Debentures
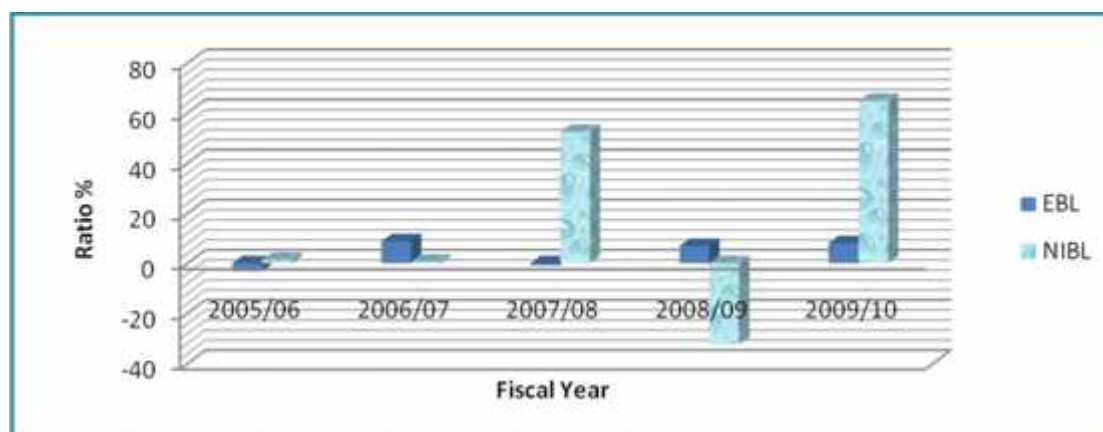
4.1.7 Return on Inter Bank Lending

The purpose of interbank lending is to gain interest income. The interest income earned by the bank in both domestic and foreign lending has been summed up and presented in the table to evaluate the return on interbank lending.

Table 4.7

Return on Inter Bank Lending

| FY	EBL			NIBL		
	Int.	**IBL**	**ROIBL**	**Int.**	**IBL**	**ROIBL**
2005/06	18.28	632.82	2.89	103.19	3062.83	3.37
2006/07	37.95	260.60	14.56	166.07	3214.03	5.17
2007/08	22.00	138.40	15.90	156.92	3664.48	4.28
2008/09	25.49	702.00	3.63	172.09	4807.54	3.58
2009/10	33.88	553.52	6.12	142.50	4370.33	3.26
Mean			**8.62**			**3.93**
S.D.			**5.52**			**0.71**
C.V.%			**64.01**			**18.13**

(Source: Appendix-III)

The table depicts that although both banks have invested in interbank lending, the interest income in such lending is fluctuating. EBL has received the interest

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on interbank lending amounting to Rs. 18.28 millions, Rs. 37.95 millions, Rs. 22.00 millions, Rs. 25.49 millions and Rs. 45.23 millions in the fiscal year 2005/06, 2006/07, 2007/08, 2008/09 and 2009/10 respectively. Consequently the return on interbank lending is 2.89% in the fiscal year 2005/06, 14.56% in the fiscal year 2006/07, 15.90% in the fiscal year 2007/08, 3.63% in the fiscal year 2008/09 and 6.12% in the fiscal year 2009/10. In average the bank has generated 8.62% return on interbank lending with the variation of 64.01%.

Similarly, NIBL has earned interest income of Rs. 103.19, Rs. 166.07 millions, Rs. 156.92 millions, Rs. 172.09 millions and Rs. 142.50 millions from interbank lending, especially from foreign bank lending, in the fiscal year 2005/06, 2006/07, 2007/08, 2008/09 and 2009/10 respectively. However, the return on interbank lending of NIBL is in fluctuating trend, and thus it is 3.37%, 5.17%, 4.28%, 3.58% and 3.26% in the fiscal year 2005/06, 2006/07, 2007/08, 2008/09 and 2009/10 respectively. In average, the bank has earned 3.93% of the total interbank lending as interest income with the variation of 18.13%.

Comparing the banks, it can be assumed that the investment on interbank lending of EBL is superior to that of NIBL, since the amount of interbank lending of EBL is lower than that of NIBL, the return is higher in EBL. Further, it would be better if EBL considers equally also on local licensed institutions for interbank lending.

Figure 4.7

Return on Inter Bank Lending
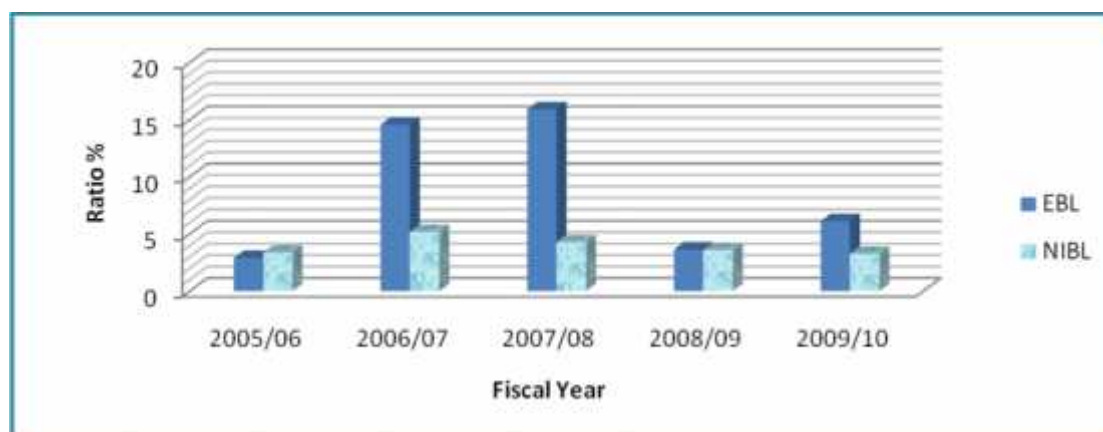
4.1.8 Provision on Investment

As per the provision of the NRB, the bank has to keep provision of investment when the market price of the invested corporate shares becomes lower than the par value. Thus, the provision on investment in relation to the total investment of the observed banks is evaluated under this heading.

Table 4.8

Provision on Investment

FY	EBL			NIBL		
	Prov.	**TI**	**Ratio**	**Prov.**	**TI**	**Ratio**
2005/06	0.80	4201.32	0.02	0	5602.87	0.00
2006/07	0.80	4985.12	0.02	0	6505.68	0.00
2007/08	1.60	5061.16	0.03	5.40	6879.42	0.08
2008/09	1.60	5950.08	0.03	3.30	7403.11	0.04
2009/10	1.60	5009.91	0.03	3.30	8638.83	0.04
Mean			**0.03**			**0.03**
S.D.			**0.01**			**0.03**
C.V.%			**25.88**			**92.04**

(Source: Appendix-I & II)

The table delineates that there is low level market risk on the corporate shares and debentures investment of EBL, since low provisioning has been made. The

provision made for the investment in corporate shares of EBL is Rs. 0.80 millions in lowest and Rs. 1.60 millions in highest. The provisioning made by the EBL has represented 0.02% in lowest and 0.03% in highest of the total investment of EBL. In average, EBL has made 0.03% of the total investment as provision. While in NIBL, the provisioning for investment is Rs. 5.40 millions in the fiscal year 2007/08, Rs. 3.30 millions in the fiscal year 2008/09 and 2009/10. Such provisioning has represented 0.08% in highest of the total investment and 0.04% in lowest of the total investment, and in average the ratio is 0.03%. Thus, it can be assumed that the corporate share and debenture investment of NIBL has equal market risk to that of EBL.

Figure 4.8

Provision on Investment
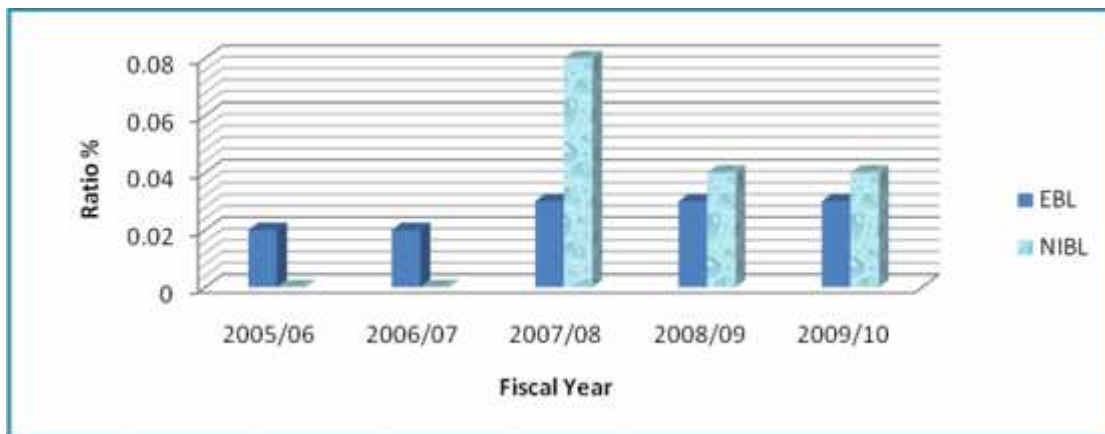
4.1.9 Statistical Analysis

Under this section, the effect of the investment of the banks in different categories on the net profit, and the estimated value of total net investment and net profit for the forthcoming four fiscal years have been evaluated. For this, mainly the correlation coefficient, probable error, and regression analysis and trend analysis have been conducted.

4.1.9.1 Relationship between Investment on Government Securities and Net Profit

To measure the impact of investment on government securities on net profit, the correlation coefficient has been evaluated and for the regression analysis, the net profit has been assumed as the dependent variable on investment on government securities.

Table 4.9

Relationship between Investment on Government Securities and Net Profit

Bank	r	P.E.	6 P.E.	Regression	Remarks
EBL	0.3911	0.2555	1.5330	NP = -220.72 + 0.16 IOGS	Insignificant
NIBL	0.6830	0.1609	0.9657	NP = -370.77 + 0.36 IOGS	Insignificant

(Source: Appendix IV)

The table signifies that there exists positive relationship between investment on government securities and net profit in EBL and in NIBL. In other words, the net profit of EBL and NIBL increases with the increase in investment in government securities of the respective banks. The 'r' value calculated between these two variables is 0.3911 and 0.6830 in EBL and NIBL respectively. Further the regression analysis indicates that the net profit of EBL increases by Rs. 0.16 millions with Rs. 1 million increase in government securities, if the variable -220.72 remains constant, and the net profit of NIBL increases by Rs. 0.36 millions with Rs. 1 million increase in government securities, if the variable -370.77 remains uniform. However, the relationship between these two variables is statistically insignificant, as the absolute value of 'r' (0.3911) of EBL is lower than the 6 P.E. (1.5330) and the absolute value of 'r' (0.6830) of NIBL is lower than its 6 P.E. (0.9657). Thus, the increment in government securities certainly may not cause net profit to increase in both the banks.

4.1.9.2 Relationship between Investment on Corporate Shares & Debentures and Net Profit

The correlation coefficient, probable error and the regression analysis between the investment on corporate share and debentures and net profit are presented in the table below.

Table 4.10

Relationship between Investment on Corporate Shares & Debentures and Net Profit

Bank	r	P.E.	6 P.E.	Regression	Remarks
EBL	0.8364	0.0906	0.5437	NP = 174.61 + 4.59 IOCSD	Significant
NIBL	0.8721	0.0722	0.4334	NP = 31.14 + 14.60 IOCSD	Significant

(Source: Appendix IV)

As expected, the relationship between investment on corporate shares & debentures and net profit of both the banks is positive, indicating that the net profit increases/decreases with the increase/decrease in investment on corporate shares and debentures. The calculated 'r' value between these two variables is 0.8364 in EBL and 0.8721 in NIBL. Further, the regression analysis signals that Rs. 1 increase in investment in corporate shares and debentures leads to Rs. 4.59 increase in net profit of EBL and Rs. 14.60 increase in net profit of NIBL, if the corresponding a-coefficient remains constant. Moreover, the relationship between these two variables could be statistically justified in both the banks, as the 'r' value of EBL is higher than the 6 P.E. and the 'r' value of NIBL is also higher than the 6 P.E. Thus, the investment in corporate shares and debentures has great impact in net profit in both the banks.

4.1.9.3 Relationship between Investment on Interbank Lending and Net Profit

Assuming net profit as the dependent variable on investment on interbank lending, the effect of investment in interbank lending on net profit has been evaluated with the aid of correlation and regression analysis.

Table 4.11

Relationship between Investment on Interbank Lending and Net Profit

Bank	r	P.E.	6 P.E.	Regression	Remarks
EBL	0.3127	0.2722	1.6329	NP = 347.62 + 0.31 IOIBL	Insignificant
NIBL	0.8338	0.0919	0.5517	NP = -781.58 + 0.40 IOIBL	Significant

(Source: Appendix IV)

The table manifests that investment in interbank lending has positive relationship with net profit of the corresponding banks, which means that the interbank lending augments the net profit of the bank. In addition, the calculated 'r' value between these two variables is 0.3127 in EBL and 0.8338 in NIBL. Also the regression analysis clarifies that per rupee increment in interbank lending leads to Rs. 031 increment in net profit of EBL, and Rs. 0.40 increment in net profit of NIBL. Thus, the effect of interbank lending is higher in NIBL than in EBL. The relationship between these two variables in NIBL is also buttressed by the high value of 'r' than the corresponding 6 P.E. However, in EBL the 'r' value is lower than the 6 P.E., indicating that the increment in inter bank lending does not always cause to increase profit.

4.1.9.4 Trend Analysis of Total Net Investment

To estimate the value of total net investment in the forthcoming four fiscal years, the trend analysis has been conducted, assuming total net investment as the dependent variable on year.

Table 4.12

Trend Analysis of Total Net Investment

Fiscal Year	EBL	NIBL
2010/11	5814.16	9091.42
2011/12	6072.14	9787.36
2012/13	6330.11	10483.31
2013/14	6588.09	11179.25
Regression Y =	**4266.31 + 257.98 X**	**4915.75 + 695.95 X**

(Source: Appendix V)

Presuming that the investment of the banks depends upon the time period, it has been ascertained that the investment of the both the banks has positive relationship with the time period. In other word, the bank continues to increase the investment in forthcoming years. As a result, the investment of EBL increases by Rs. 257.98 million per year and that of NIBL increases by Rs. 695.95 million per year in the future. This indicates that the pace of growth in investment of NIBL will be greater than that of EBL. In addition, the estimated value of investment by the end of the fiscal year 2013/14 will be Rs. 6588.09 millions and that of NIBL will be Rs. 11179.25 million.

Figure 4.9

Trend Analysis of Total Net Investment
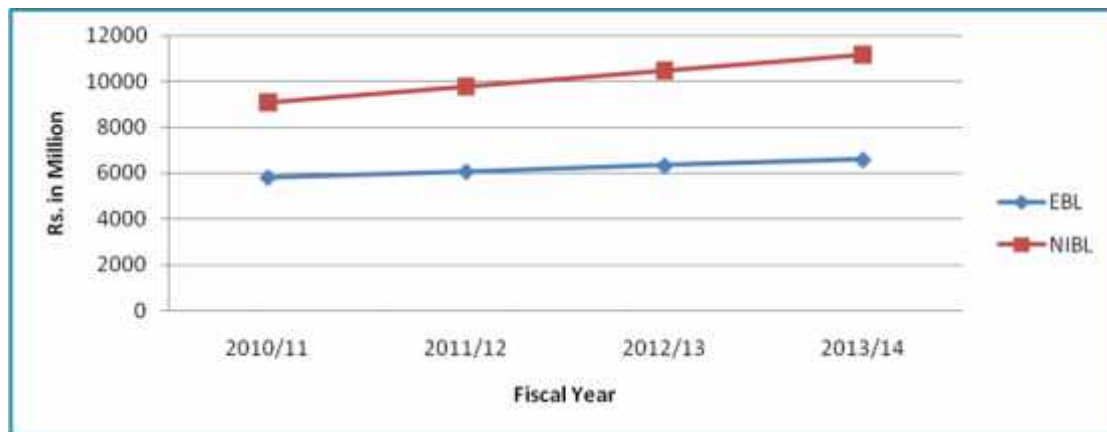
4.1.9.5 Trend Analysis of Net Profit

Let the dependent Variable, Net Profit be denoted by Y and the independent variable, Year be denoted by X. Then, the regression equation of Net Profit on Year, along with the estimate value of net profit for the forthcoming four fiscal years is presented in the below table.

Table 4.13

Trend Analysis of Net Profit

Fiscal Year	EBL	NIBL
2010/11	950.46	1412.06
2011/12	1103.59	1635.06
2012/13	1256.71	1858.07
2013/14	1409.84	2081.07
Regression Y =	**31.70 + 153.13 X**	**74.04 + 223 X**

(Source: Appendix V)

The table reveals that the net profit of the bank will continually increase in the forthcoming year as well. The net profit of the EBL will be Rs. 1409.84 million and that of NIBL will be Rs. 2081.07 million by the end of the fiscal year 2013/14. Also, the regression analysis between net profit and time period shows that the increment of net profit per year will be greater in NIBL than in EBL. The net profit of EBL increases by Rs. 153.13 million, if the variable 31.70 remains constant, and the net profit of NIBL increases by Rs. 223 million, if the variable 74.04 remains stable.

Figure 4.10

Trend Analysis of Net Profit
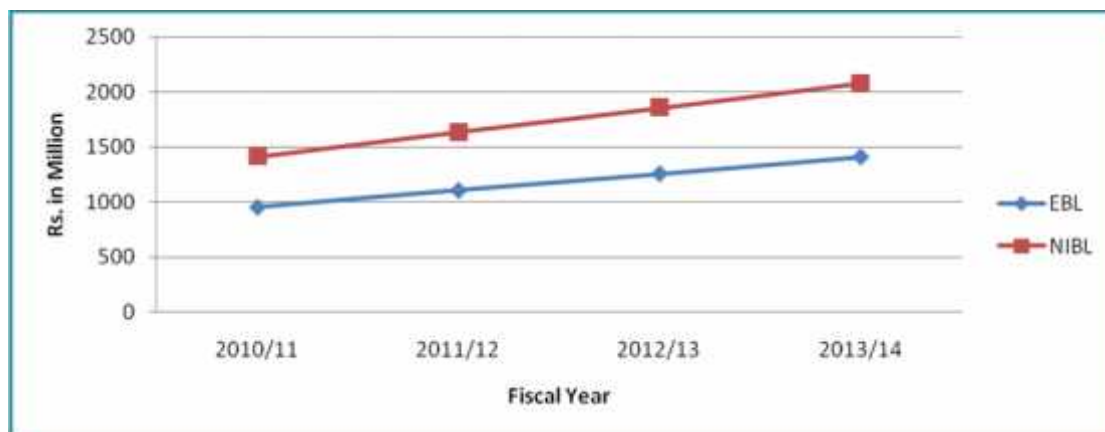
4.2 Primary Data Analysis

To understand the opinions of the investors and employees with regard to investment policy, and the requirement for enhancement of investment, the

primary data analysis has been conducted. For analyzing the primary data, a questionnaire containing 8 questions has been prepared and requested to the 15 employees of NIBL and EBL, and 15 investors at the NEPSE floor for expressing their views.

4.2.1 Appropriateness of Investment Policy

To scrutinize whether the existing investment policy adopted by the banks is appropriate to meet the goal of the bank, the respondents are asked to express their opinions. The collected opinions are tabulated in the table below.

**Table 4.14**

Appropriateness of Investment Policy

Response	Employee		Investors		Total	
	No.	%	No.	%	No.	%
Yes	8	53	4	27	12	40
No	6	40	11	73	17	57
Don't Know	1	7	0	0	1	3
Total	**15**	**100**	**15**	**100**	**30**	**100**

(Source: Opinion Survey, 2011)

The table reveals that 53% (8 out of 15) of the employees, 27% (4 out of 15) of the investors and 40% (12 out of 30) of the total respondents are in the view that the investment policy adopted by EBL and NIBL is appropriate. In contrast to this opinion, 40% (6 out of 15) of the employees, 73% (11 out of 15) of the investors, and 57% (17 out of 30) of the total respondents have stated that the current investment policy adopted by the banks in not appropriate and needs to be amended. However, 7% of the employees, which represents 3% of the total respondents, have stated that they have no idea on this issue. Palpably, on the basis of the overall majority, and the majority of each category, it can be derived that the investment policy of the banks necessitates restructuring for enhancement.

Figure 4.11

Appropriateness of Investment Policy
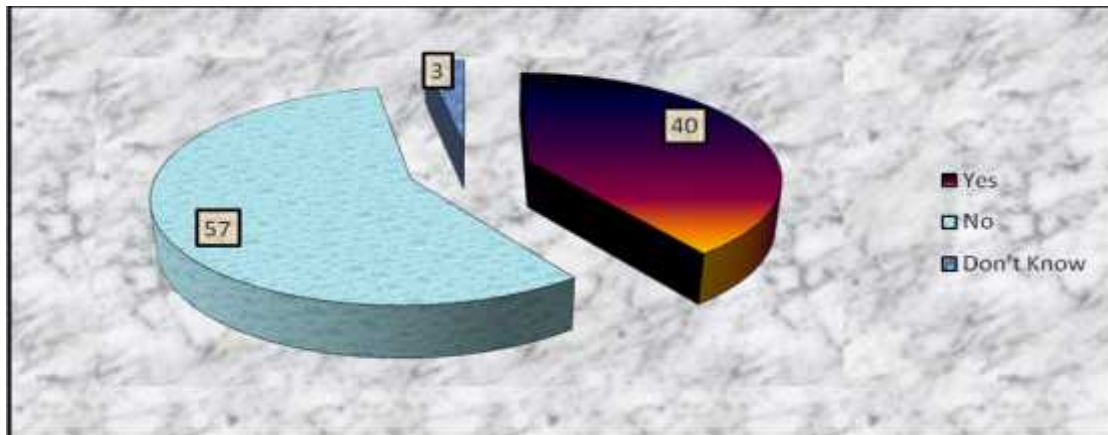
4.2.2 Priority in Making Investment

The secondary data has revealed that the banks have given predilection to government securities for investment. To examine on which area of investment, the bank should show much interest, the respondents are asked to present their opinions.

Table 4.15

Priority in Making Investment

| Response	Employee		Investors		Total	
	No.	%	No.	%	No.	%
Equity Securities	4	27	6	40	10	33
Short-term Debt Securities	3	20	3	20	6	20
Long-term Debt Securities	2	13	1	7	3	10
Derivative Securities	1	7	2	13	3	10
Real Assets	3	20	3	20	6	20
Other Investment Alternatives	2	13	0	0	2	7
Total	**15**	**100**	**15**	**100**	**30**	**100**

(Source: Opinion Survey, 2011)

It has been ascertained that the 27% of the employees, 40% of the investors, and in total 33% of the total respondents are in the view that the bank should give most priority to equity securities, which incorporates common stock and

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preferred stock, while making investment. Similarly, 20% of the employees, 20% of the investors, and 20% of the total respondents have stated that the bank should give more priority to short-term debt securities, which encompasses T-Bill, Commercial paper, Banker's Acceptance etc, in making investment. Likewise, 13% of the employees, 7% of the investors, and 10% of the total respondents have the bank should give predilection to long-term debt securities, which includes T-Notes, T-Bonds, Savings Bonds etc. Moreover, 7% of the employees, 13% of the investors and 10% of the total respondents have opined that the bank should prefer to derivative securities, which involves options, commodity, rights, warrants, futures and so on.

In addition, 20% of the employees, 20% of the investors, and 20% of the total respondents have opined that the bank should give main priority to investment in real assets, which includes precious metal, real estate, collectibles etc. Finally, 13% of the employees, which represents 7% of the total respondents, have stated that the bank should give preference to other investment alternatives, which involves pension funds, mutual funds etc. Consequently, on the basis of the overall majority, it can be stated that the bank should give more priority to equity investment for enjoying more profit.

Figure 4.12

Priority in Making Investment
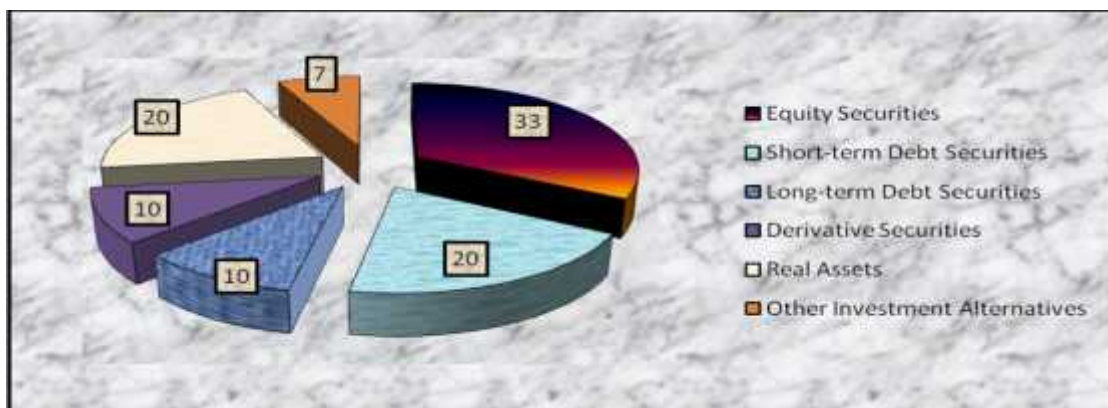
4.2.3 Sensitivity of Investment Process

Investment process of the bank augments the profit and reduces the risk, if applied effectively. To investigate on which factor the investment process should be more sensitive, the respondents are asked on this issue. The responses obtained through questionnaire on this issue are presented in the below table.

Table 4.16

Sensitivity of Investment Process

Response	Employee		Investors		Total	
	No.	%	No.	%	No.	%
Setting Investment Policy	4	27	6	40	10	33
Performing Security Analysis	6	40	3	20	9	30
Constructing a Portfolio	1	7	1	7	2	7
Revising the Portfolio	2	13	3	20	5	17
Evaluating Portfolio Performance	2	13	2	13	4	13
Total	**15**	**100**	**15**	**100**	**30**	**100**

*(Source: Opinion Survey, 2011)*

The investment process should be more sensitive while setting investment policy, as per the view of 27% of the employees, 40% of the investors, and 33% of the total respondents. Similarly, 40% of the employees, 20% of the investors, and 30% of the total respondents have stated that the investment process should be more sensitive toward conducting the analysis of security. Likewise, 7% of the employees, 7% of the investors, and 7% of the total respondents have said that the investment process should reflect constructing an effective portfolio.

While 13% of the employees, 20% of the investors, and 17% of the total respondents have stated that the investment process should be more sensitive in restructuring the portfolio. Finally, 13% of the employees, 13% of the investors, and 13% of the total respondents have affirmed the sensitiveness of investment process in evaluating the portfolio performance. Considering the

overall majority, it can be assumed that the investment process should be more sensitive toward creating the investment policy.

Figure 4.13

Sensitivity of Investment Process
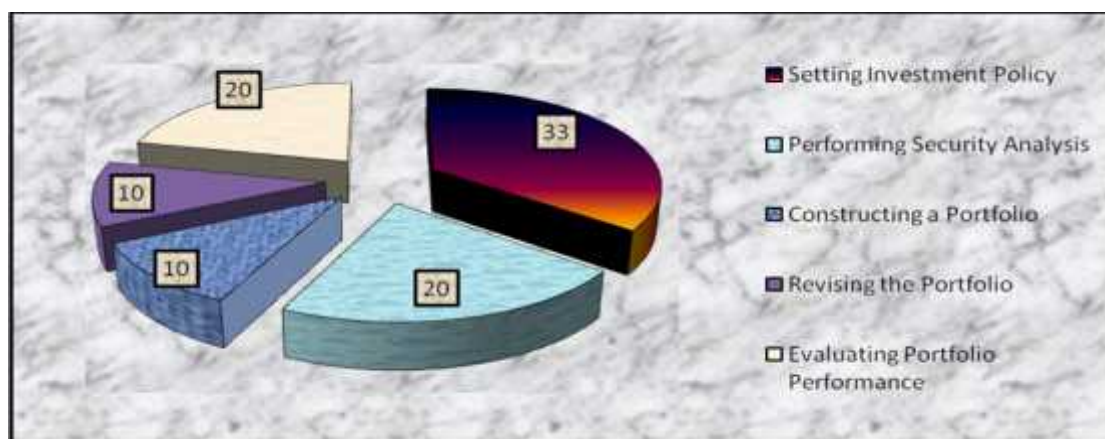
4.2.4 Crucial Element in Equity Share Investment

To analyze the crucial element that fascinates the bank for investment is ubiquitous. Thus, to examine on which element do the most banks focuses while taking decision for investment, the respondents are asked on this matter.

Table 4.17

Crucial Element in Equity Share Investment

| Response	Employee		Investors		Total	
	No.	%	No.	%	No.	%
Dividend Pattern	3	20	3	20	6	20
Earnings Per Share	2	13	1	7	3	10
Right Offerings	3	20	2	13	5	17
Capital Gain/Loss	7	47	9	60	16	53
Total	**15**	**100**	**15**	**100**	**30**	**100**

(Source: Opinion Survey, 2011)

The table explores that as per the opinion of 20% of the employees, 20% of the investors and 20% of the total respondents, the bank considers the dividend payment policy of the licensed institutions as the most crucial element while making investment in equity shares. Further, 13% of the employees, 7% of the

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investors, and 10% of the total respondents are in the view that the bank considers earnings per share of the licensed institutions as the major element for investment.

Similarly, 20% of the employees, 13% of the investors, and 17% of the total respondents have opined that the right offerings practices of the licensed institutions is the most crucial element for bank while making investment in equity shares. Likewise, 47% of the employees, 60% of the investors, and 53% of the total respondents have stated that the capital gain/loss that is going to be achieved in the future is the main crucial element that the bank considers while making investment in equity shares. Thus, on the basis of the majority of each category, and the overall majority, it can be said undoubtedly that that capital gain/loss is the most crucial element for investment.

Figure 4.14

Crucial Element in Equity Share Investment
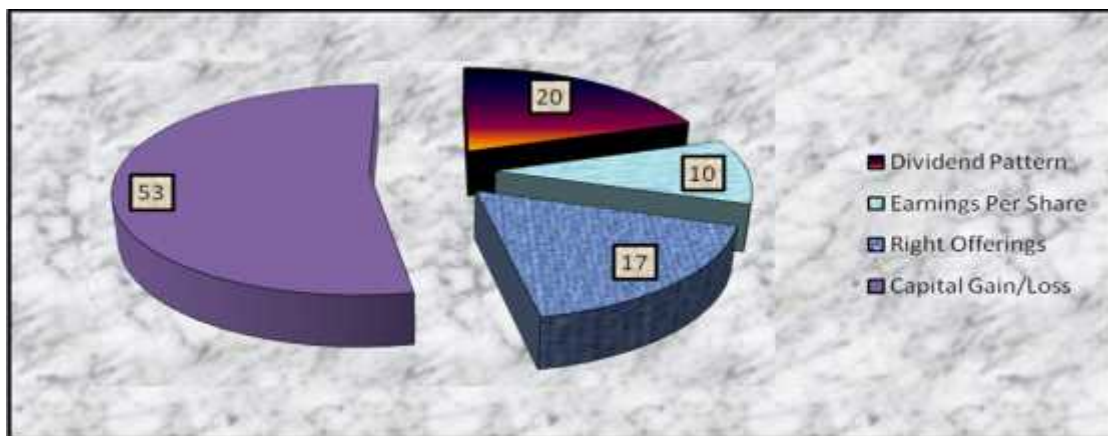
4.2.5 Suitability of Investment Directive of NRB

NRB is the regulating and monitoring body of Nepalese financial institutions. Thus the role of NRB is crux for smooth operation of banking. Hence, to examine whether the investment directive issued by NRB is appropriate with the existing market situation, the respondents are requested to express their views.

Table 4.18

**Suitability of Investment Directive of NRB**

Response	Employee		Investors		Total	
	No.	%	No.	%	No.	%
Yes	8	53	5	33	13	44
No	6	40	10	67	16	53
Don't Know	1	7	0	0	1	3
Total	**15**	**100**	**15**	**100**	**30**	**100**

(Source: Opinion Survey, 2011)

The table delineates that the majority of the employees, 53%, are in the opinion that the investment directive of NRB befits the necessity of current market situation. However, 67% of the investors contradicts on this issue, and says that the investment directive of NRB is not suitable in the present market. Similarly, 40% of the employees have stated that investment directive of NRB is not suitable, and 33% of the investors have stated that it befits the market requirement. Moreover, 7% of the employees have stated that they have no idea on this issue. In overall, 44% of the total respondents have avowed that the investment directive is suitable and 53% of the respondents have resisted that it is not suitable, and 3% of the respondents have remained neutral. Considering the overall majority, it would be worthwhile if NRB scrutinizes its investment policy and then directs better investment strategy.

Figure 4.15

Suitability of Investment Directive of NRB
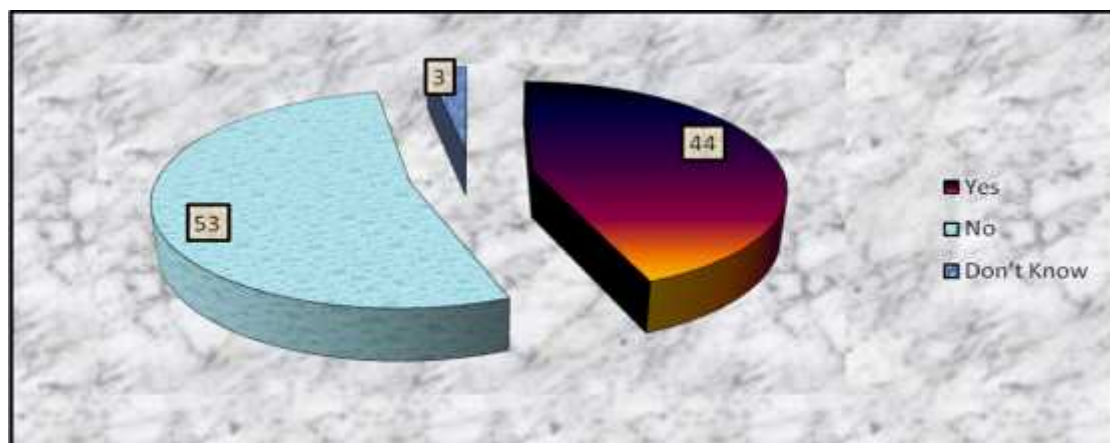
4.2.6 Necessity of Strengthening for Optimum Investment Policy

For having optimum investment policy, the banks need to be strong enough in each of its activity. To inspect on which area the bank needs to strengthen most, the respondents are asked on this issue. The collected responses are presented in the table below.

Table 4.19

Necessity of Strengthening for Optimum Investment Policy

Response	Employee		Investors		Total	
	No.	%	No.	%	No.	%
Decision Making Authority	3	20	7	47	10	33
Productivity of Employee	2	13	0	0	2	7
Capital	4	27	2	13	6	20
Risk Assessment Mechanism	6	40	6	40	12	40
Total	**15**	**100**	**15**	**100**	**30**	**100**

*(Source: Opinion Survey, 2011)*

The table shows that 20% of the employees and 47% of the investors have opined that the decision making authority for investment necessitates to be restructured or be more capable for producing optimum investment policy. Similarly, 13% of the employees and 0% of the investors enforced on strengthening the productivity of the bank's employees for having optimum investment policy. Likewise, 27% of the employees and 13% of the investors have emphasized to strengthen the bank capital for having sound investment policy. Moreover, 40% of the employees and 40% of the investors have opined to strengthen the risk assessment mechanism of the bank for optimum investment policy.

Summing the responses of each category, it has been ascertained that 33% of the total respondents have pointed out decision making authority, 7% have pointed out productivity of employees, 20% have stated on capital and 40% have opined risk assessment mechanism needs to be strengthened for having sound optimum investment policy. Thus, considering the overall majority, it

can be concluded that the bank needs to strengthen the risk assessment mechanism most for creating sound investment policy.

Figure 4.16

Necessity of Strengthening for Optimum Investment Policy
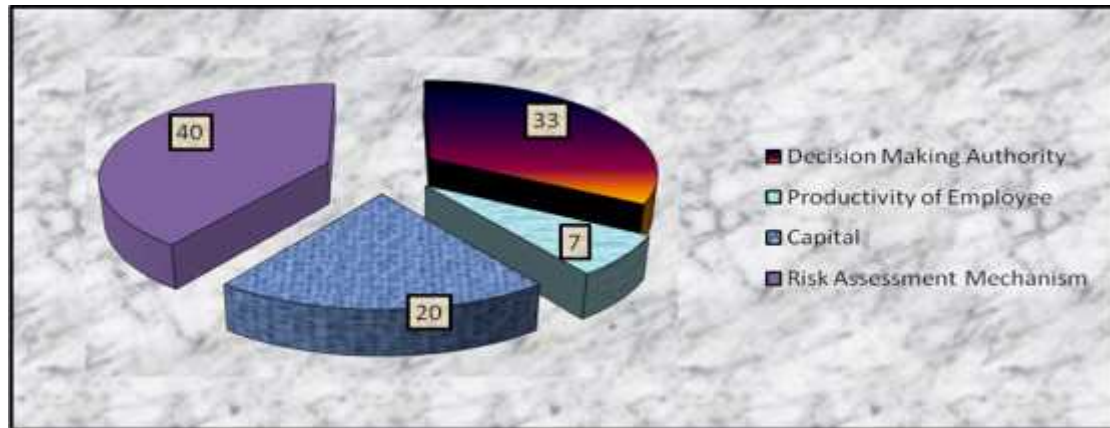
4.2.7 Main Reason for Low Proportion of Investment

The secondary data analysis has verified that the proportion of investment on total fund mobilization is low, especially in comparison to the loan and advances. To trace out the main reason on the bank's less interest on investment, the question has been prepared and presented to the respondents.

Table 4.20

Main Reason for Low Proportion of Investment

| Response	Employee		Investors		Total	
	No.	%	No.	%	No.	%
Because of Legal Barriers	1	7	0	0	1	3
Because of High Risk	4	27	5	33	9	30
Because of Low Profitability	5	33	7	47	12	40
Because of Maturity Period of Bond	3	20	2	13	5	17
Because of Ineffectiveness of SEBON	2	13	1	7	3	10
Total	**15**	**100**	**15**	**100**	**30**	**100**

(Source: Opinion Survey, 2011)

The majority of both the employees, 33%, and the investors, 47%, are in the view that because of low profitability sector, the investment is low as compared to loan and advance disbursement. While 7% of the employees have blamed that the legal requirements obstructs the bank in increasing the investment amount. Further 27% of the employees and 33% of the investors have opined that since the investment carries high risk, the investment amount is lower than the loan and advances. In addition, 20% of the employees and 13% of the investors have stated that the maturity period of bond, a major investment sector, is long, as a result the bank shows less interest in investment than in granting loan and advances. Likewise, 13% of the employees and 7% of the investors have opined that the ineffectiveness of SEBON in smooth operation of securities trading is one most crucial reason behind the low interest of bank in investment.

In overall, 3% of the respondents have accused legal obstacles, 30% of the respondents have shown high risk, 40% of the respondents have stated low profitability, 17% of the respondents have pointed out maturity period of bond and 10% of the respondents have blamed SEBON for its ineffectiveness. Considering the majority of each category and the overall majority, it can be inferred that the investment of bank returns low profit, as a result the banks are more enticed in granting loan and advances than making investment.

Figure 4.17

Main Reason for Low Proportion of Investment
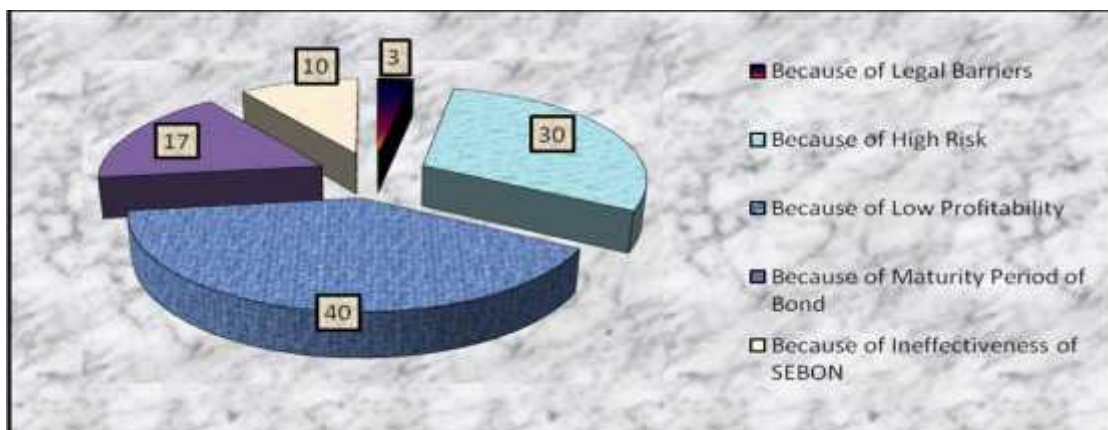
4.2.8 Suggestion for Optimum Investment Policy

At the end of the questionnaire, the respondents are asked to provide suggestions that will enhance the banks' investment policy. The recommendations obtained from them in having optimum investment policy are presented in the below table.

Table 4.21

Suggestion for Optimum Investment Policy

Response	Employee		Investors		Total	
	No.	%	No.	%	No.	%
Diversify the Investment	3	20	7	47	10	33
Make Meticulous Assessment of Associated Risk	4	26	1	7	5	17
Evaluate Profitability and Capital Gain	6	40	2	13	8	27
Increase Investment Weight	1	7	3	20	4	13
Quest Alternate Investment Opportunity	1	7	2	13	3	10
Total	**15**	**100**	**15**	**100**	**30**	**100**

(Source: Opinion Survey, 2011)

The majority of the employees have suggested the bank to meticulously evaluate the profitability and capital gain from the investment for having optimum investment policy. About 40% of the total employees have opined this view. In contrast, only 13% of the investors have suggested this point. Likewise, the majority of the investors, 47%, and 20% of the employees have strongly suggested the bank to diversify the investment, which means not to be saturated to government securities, for having optimum investment policy. Similarly, 26% of the employees and 7% of the investors have emphasized on making meticulous assessment of associated risk with investment for having sound investment policy. Moreover, 7% of the employees and 20% of the investors have stated that the investment proportion on total fund mobilization is low and thus the bank should increase the weight of the investment for having optimum investment policy. Finally, 7% of the employees and 13% of

the investor have urged that the bank should quest alternate investment opportunity for buttressing the investment policy.

In overall, 33% of the total respondents have suggested diversification of the investment, 17% have opined conducting careful examination of associated risk with investment, 27% have suggested evaluating profitability and capital gain on investment, 13% have stated enforced on the increment in investment weight, and 10% have suggested questing alternate investment opportunity. Thus it would be better if the bank considers all these valuable suggestions, mainly on the diversification of investment, for having optimum investment policy.

Figure 4.18

Suggestion for Optimum Investment Policy
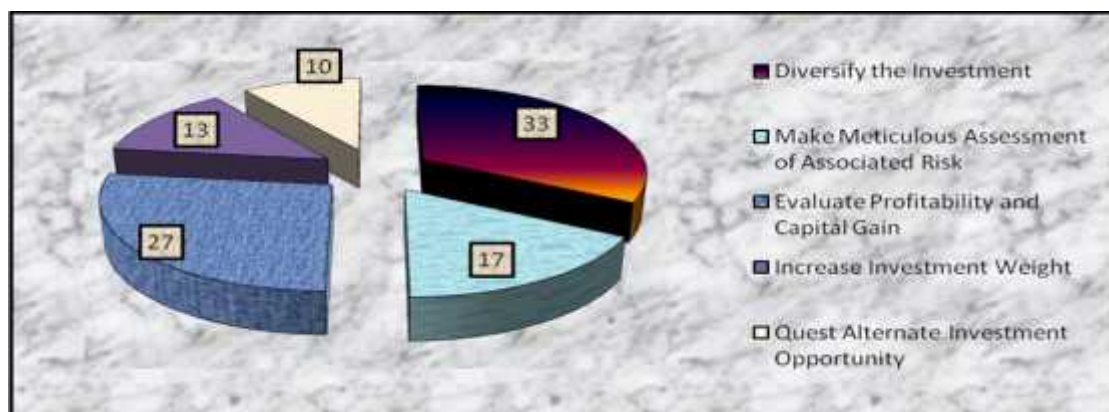
4.3 Major Findings of the Study

On the basis of the analyses made on the previous sections, the following major findings have been drawn;

Findings from Secondary Data Analysis

⟩ Both the banks have given low preference to investment, which indicates that the bank relies mainly on loan and advances for generating income. The average total net investment to total assets is just 19.29% in EBL and 19.31% in NIBL.

⟩ The investment in government securities to total investment is 89.50% in EBL and 44.75% in NIBL in average. Among the various government securities, the treasury bill occupies major portion.

⟩ NIBL has not invested in corporate debenture, while EBL has invested in both corporate shares and corporate debenture from the fiscal year 2007/08. Nonetheless the investment in corporate shares and debentures is comparatively very low to government securities. In average, the investment in corporate shares and debentures to total investment of EBL is 1.32% and NIBL is 0.67%.

⟩ EBL has neglected local interbank lending in most of the years. The interbank lending to total investment of EBL is 9.17% and that of NIBL is 54.57% in average.

⟩ The investment in government securities has yielded 4.07% interest income in EBL and 3.69% interest income in NIBL. Besides these, the average return on investment in corporate shares and debentures of NIBL is higher than that of EBL. The average return on corporate shares and debentures of EBL is 3.90% and that of NIBL is 17.38%. In addition, the average return on inter bank lending of EBL is 8.62% and that of NIBL is 3.93%.

⟩ Both the bank has maintained provision for investment. Astonishingly, both the banks have maintained 0.03% of the total investment as the provision for probable loss on investment.

⟩ The statistical analysis reveals that government securities have insignificant effect and corporate share and debenture has significant effect on net profit of both the banks. However, interbank lending has insignificant effect on net profit of EBL and significant effect on net profit of NIBL.

⟩ The estimated value of total net investment for the fiscal year 2013/14 will be Rs. 6588.09 million in EBL and Rs. 11179.25 million in NIBL. Likewise, the trend value of net profit in same year will be Rs. 1409.84 million in EBL and Rs. 2081.07 million in NIBL.

Findings from Primary Data Analysis

⟩ The majority of the respondents, 57%, have opined that the banks are practicing inappropriate investment policy. Further, 33% of the respondents have stated that the bank should give more priority to equity securities while making investment.

⟩ 33% of the respondents have said that the investment process should be more sensitive toward setting the investment policy. And 53% of the respondents have claimed that the bank analyzes capital gain/loss on equity shares most while making decision to invest.

⟩ In addition, 53% of the respondents have informed that the NRB directives related to the investment does not match with the current market situation and thus is unsuitable. Similarly, 40% of the respondents have stated that the bank should strengthen its risk assessing mechanism for having optimum investment policy.

⟩ Likewise, 40% of the respondents have stated that the bank shows less interest in investment due to the low profitability it carries in comparison to the other ways of earning income. Finally, 33% of the respondents have suggested the bank to diversify the investment, i.e. not to be saturated on government securities only, in order to have optimum investment policy.

CHAPTER – V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

Designing good investment policy helps to the improvement of investment policy in the country. As political influence, intervention economic scenario and social, economic scenario of the country is dramatically problem for the detection of designing investment policy of bank. Investment policy plays a key role on the development of countries utmost investment.

The political insanity, government rules, tax policy treaty with neighbor country, social and economic condition of the country affect investment policy of bank. To keep up the stability with the foreign policy results the improvement of investment policy.   Government policy affects the investment policy of the company, bank and institution. Government intervention in investment policy is custom tariff initiated by the government policy, VAT refund policy and tax holding policy including duty taxes i.e. export and import directly influences investment policy.

Analysis of investment to avoid the risk, risk related investment influence the financial and economic condition of investment. Technical and marketing analyses too reflect the risk measurement. As the investor, the adequate knowledge of investment policy is required. Major problem for applying the investment policies are integrator of the consumer, changing policy of the country, industrial policy and neighbor country's policy. To examine the

investment policy practiced in the commercial banks in Nepal, two banks namely, Everest Bank Limited and Nepal Investment Bank Limited, have been chosen as sample. The main objective of the study is to examine the investment policy of the selected banks. The study uses the both financial tools and statistical tools to achieve the objective. Further, the study uses both the secondary and primary data.

5.2 Conclusion

From secondary data analysis, it can be considered that the mobilization in investment occupies crucial ramifications of total assets in banking sector, though such mobilization is lower than the mobilization in granting loan and advances. Categorically, NIBL has remained more dependent than EBL in mobilization of total fund in investment. More concisely, it can be assumed that the banking industry is more allured toward the Treasury bill than toward the development bond and savings bond. Among the various investments, EBL has given more preference to government securities, while NIBL has given more preference to inter bank lending. Between the observed banks, it can be ideally surmised that EBL has focused more on government securities than NIBL. Besides these, it can be genuinely speculated that EBL has given more preference to corporate share and debenture investment than NIBL, as a result the preponderance of corporate share and debenture on total investment in EBL is higher than that in NIBL. Generally, it can be said that each bank has preferred to corporate shares and debentures at last, then to interbank lending and government securities. In addition, it can be inferred that the investment of EBL in government securities is more lucrative than that of NIBL. This might be due to policy of EBL in investing on development bonds and in increasing the treasury bills, while in contrast NIBL has adopted the policy of not making investment in development bonds.

Further, although the corporate shares and debentures to total investment of EBL is higher than that of NIBL, NIBL has remained to yield high percentage of average return on corporate shares and debentures. However, the investment on interbank lending of EBL is money-spinning to that of NIBL, though the inter bank lending to total investment of EBL is lower than that of NIBL. Statistically, it can be derived that the increment in corporate shares and debentures certainly increases the net profit of both the banks, and it cannot be ensured that the increment in government securities increases the net profit of both the banks. In addition, the investment in interbank lending has statistically positive relationship with net profit of NIBL only, which means that the interbank lending augments the net profit of such bank.

From primary data analysis, it can be stated that the investment policy adopted by the observed banks is not ideal, and thus demands amendment. The banks have given equity securities more preference to other sectors like debt securities, derivative securities, real assets and others. Among the others, the setting of investment policy is more sensitive rather than analyzing security deposited and others. Further, capital gain/loss is the major concern for the banks while making investment, rather than the dividend and right offerings. Most of the personnel of the banks are in the view that the directive of NRB regarding investment is not pragmatic and needs. To strengthen the investment policy, the bank needs to review the risk assessment mechanism and should change if necessary. It has been ascertained that the lower profitability in investment has caused the banks to be more attractive toward loan and advances in generating profit. Finally, it can be concluded that the diversification of investment would be better for having optimum investment policy.

5.3 Recommendations

On the basis of the analysis, the following recommendations have been provided for the enhancement of banking investment;

⌡ NRB should set directive that would be suitable for the banks and would be pragmatic for the banks to adopt.

⌡ As the return on investment is not always clear, so the banks need to prepare the strategy so as to face the ongoing challenges in investment. A balanced investment strategy is generally required in the process of investment, which possesses long time period and some risk tolerance.

⌡ An investment strategy in mutual funds is probably the best bet for a profitable investment. Mutual fund is a pool of money supplied by different investors and in turn used by the mutual fund company to invest in various assets such as stocks and bonds. However, a detailed research has to be conducted by the bank for choosing the mutual fund companies and only those should be considered which have a professional investment manager.

⌡ The mobilization of fund in investment is lower than that in loan and advances. It would be worthwhile if EBL and NIBL recognize the investment that is lucrative and mobilize the fund in portfolio basis.

⌡ Both the banks have given high priority to the government securities while making investments, however, the return on inter bank lending is greater than that of government securities. It would be worthwhile if both the banks divert more investment amount to inter bank lending.

⌡ Further, NIBL and EBL need to trace out the method for reducing risk in corporate shares and debentures and thereby decrease the provision needed for such risk.

⌡ Each bank should identify the much risky assets of portfolio and thus try to reduce the investment amount on that sector and increase the investment amount in other secured assets.

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APPENDIX - III
Return on Investment

Everest Bank Limited

A)   EBL Interest on Investment

S.N.	Details		2005/06	2006/07	2007/08	2008/09	2009/10
					Fiscal Year		
1	Government Securities		97272195	128565724	180218958	289764623	238993331
	a	Treasury Bills	84483468	114352592	114810856	205441518	144197378
	b	Development Bonds	12788727	14213132	65408102	84323105	94795953
	c	National Saving Certificates	0	0	0	0	0
2	Foreign Banks		18284106	32256018	8993070	3964916	659487
3	Nepal Rastra Bank Bond		0	0	0	0	0
4	Debenture and Bonds		0	0	0	6572826	6590859
	a	Financial Institutions	0	0	0	0	0
	b	Other Organizations	0	0	0	0	0
5	Interest on Inter Bank Lending		0	5690311	13004651	21526194	33217910
Total Interest on Investment			**115556301**	**166512053**	**202216679**	**321828559**	**279461587**

B)   Dividend on Share Price

S.N.	Details	2005/06	2006/07	2007/08	2008/09	2009/10
1	Dividend Received	161500	253920	751032	0	1510568

C)   Price Increase in Share Price

S.N.	Details	2005/06	2006/07	2007/08	2008/09	2009/10
1	**Himalayan Distillery Ltd.**					
	Previous Yr. Mkt. Value	13414000	12609160			
	Current Yr. Mkt. Value	12609160	14084700			
	Price Increase/Decrease	**-804840**	**1475540**	**0**	**0**	**0**
2	**Taragaon Regency Hotel**					
	Previous Yr. Mkt. Value			5000000	3400000	3900000
	Current Yr. Mkt. Value			3400000	3900000	3900000
	Price Increase/Decrease			**-1600000**	**500000**	**0**
Total Price Increase (1+2)		**-804840**	**1475540**	**-1600000**	**500000**	**0**

Nepal Investment Bank Limited

A) NIBL Interest on Investment

S.N.	Details		Fiscal Year				
			2005/06	2006/07	2007/08	2008/09	2009/10
1	Government Securities		82420193	78493544	99991095	140697625	169619945
	a	Treasury Bills	82420193	78493544	99991095	140697625	167872786
	b	Development Bonds	0	0	0	0	1747159
	c	National Saving Certificates	0	0	0	0	0
2	Foreign Bank		103192794	166074316	156916647	172089859	119505912
3	Nepal Rastra Bank Bond		0	0	0	0	0
4	Debenture and Bonds		0	0	0	0	0
	a	Financial Institutions	0	0	0	0	0
	b	Other Organizations	0	0	0	0	0
5	Interest on Inter Bank Lending		0	0	0	0	22992606
Total Interest on Investment			**185612987**	**244567860**	**256907742**	**312787484**	**312118463**

B) Dividend on Share Price

S.N.	Details	2005/06	2006/07	2007/08	2008/09	2009/10
1	Dividend Received	**241205**	**213323**	**832500**	**1605975**	**4329450**

C) Price Increase in Share Price

S.N.	Details	2005/06	2006/07	2007/08	2008/09	2009/10
1	**Purbanchal Gra. Bikash**					
	Previous Yr. Mkt. Value					3000000
	Current Yr. Mkt. Value					28950000
	Price Increase/Decrease			**0**	**0**	**25950000**
2	**Swalamban Bikash Bank**					
	Previous Yr. Mkt. Value			2400000	38424000	38346000
	Current Yr. Mkt. Value			38424000	13944000	48891150
	Price Increase/Decrease			**36024000**	**-24480000**	**10545150**
3	**Taragaon Regency Hotel**					
	Previous Yr. Mkt. Value			15000000	9600000	11700000
	Current Yr. Mkt. Value			9600000	11700000	11700000
	Price Increase/Decrease			**-5400000**	**2100000**	**0**

4	**Nepal Clearing House**					
	Previous Yr. Mkt. Value					125000
	Current Yr. Mkt. Value					2500000
	Price Increase/Decrease			**0**	**0**	**2375000**
Total Price Increase (1+2+3+4)		**0**	**0**	**30624000**	**-22380000**	**38870150**

APPENDIX- VI
QUESTIONNAIRE

Dear Sir/Madam,

With the intention to collect opinion regarding the "Analysis of Investment Policy of Commercial Banks (With Reference to Everest bank Limited and Nepal Investment Bank Limited)", some questions are prepared and presented to you. It would be a magnanimous of you, if you provide your valuable responses, which could illuminate a lot in fulfilling the objectives of the study.

Respondents:

Name:

Designation: Employee/Investors (Please tick one)

Bank (if Employee:

Please tick one appropriate answer.

1. Do you think that the investment policy adopted by the commercial banks of Nepal is appropriate?

   a. Yes   b. No   c. Don't Know

2. The bank should give priority to……………………….. while making investment.

   a. Equity Securities
   b. Short-term Debt Securities
   c. Long-term Debt Securities
   d. Derivative Securities
   e. Real Assets
   f. Other Investment Alternatives

3. The investment process of the present commercial bank's need to most sensitive in…………………………….
   a. Setting Investment Policy
   b. Performing Security Analysis
   c. Constructing a Portfolio
   d. Revising the Portfolio
   e. Evaluating the Portfolio Performance

4. While making investment on corporate equity shares, the bank should give more weight to………………..
   a. Dividend Pattern
   b. Earnings Per Share
   c. Right Offerings
   d. Capital Gain/Loss

5. Does the directive issued by NRB for investment befit in current market situation?
   a. Yes   b. No   c. Don't Know

6. For having best investment policy, which of the following needs to strengthen most?
   a. Decision Making Authority
   b. Productivity of Employee
   c. Capital
   d. Risk Assessment

7. Why most of the commercial banks of Nepal could not mobilize the funds in investment at least to the level of loans and advances?
   a. Because of Legal Barriers
   b. Because of High Risk
   c. Because of Low Profitability
   d. Because of Maturity Period of Bond
   e. Because of Ineffectiveness of SEBON

8. What do you suggest the bank of for having optimum investment policy?
   a. Diversify the Investment
   b. Make Meticulous Assessment of Associated Risk
   c. Evaluate Profitability and Capital Gain
   d. Increase Investment Weight
   e. Quest Alternate Investment Opportunity

                                Thank You.