Research Article

Loan and Advance Management of Nepal Bank Limited and Rastriya Banijya Bank

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ABSTRACT

The main objective of this study was to assess and compare loan and advance management of Nepal Bank Limited and Rastriya Banijya Bank. The study used descriptive and analytical research design. Two banks out of total 27 commercial banks in Nepal were selected based on judgmental sampling. Quantitative data are collected from secondary sources of annual audited report. The collected data were classified, coded and analyzed with the help of statistical tools like percentage, mean, standard deviation, coefficient of correlation, and coefficient of determination using MS-Word, MS-Excel, and Statistical Package for Social Science. Both the banks utilized most of the deposits in the forms of loan and advance. NBL has provided more amount for loan loss provision in comparison with the RBB. Non-performing loan to total loan and advance ratio showed that NBL (2.25%) has good management than the RBB (4.03%). Unlike this, the mean ratio of loan and advance to total assets ratio of NBL (55.7%) is lower than the RBB (61.48%) proved that RBB mobilized fund properly. Lower standard deviation and coefficient of variation of RBB have been indicated that the bank has more uniformity than the NBL except interest income to loan and advance ratio. The study showed that there is significant relationship of loan and advance with total deposit, loan loss provision, non-performing loan and total assets of both banks except the non-performing loan and loan and advance of RBB.

Keywords: Bank; credit; loan and advance; ratio

INTRODUCTION

Banks are considered as a heart of the financial system. The banks collect scattered money from individuals, government institutions and business units. The collected money is termed deposits. They make funds available through their lending and investing activities to borrowers, individuals, business firms and government institutions. Loan and advance management is one of the most important activities in banking industry and cannot be overlooked by any economic enterprise engaged in credit irrespective of its business nature. Sound credit management is a prerequisite for a financial institutions stability and continuing profitability, while deteriorating credit quality is the most frequent cause of poor financial performance and condition. As with any financial institution, the biggest risk in banking sector is lending money and not getting it back (Eskinder, 2016). Loan is a pre-dominate source of revenue, and effective management of loan portfolio and credit function is fundamental to banks safety and soundness (Imeokpararia, 2013).

Credit risk management is crucial on the bank performance since it has a significant relationship with bank performance and contributes up to 22.6% of the bank performance (Poudel, 2012). The major cause of the winding up of some commercial banks is their poor management of their finance and credit. Many of them were writing off huge amounts of debt yearly and also reflected some going concern issues that related to their management of credit and finance (Uwuigbe, Uwuigbe, & Oyewo, 2015). Poudel (2012) states that credit risk management is an important predictor of bank financial performance thus success of bank performance depends on risk management.

Commercial banks' loan performance could be largely attributed to the efficiency of the credit management practices put in place at the institutions. The banks have to regularly evaluate and update practices relating to debt collection policy, client appraisal and lending policy that are capable of ensuring that credit risks are identified and recorded from departmental level to the institution at large (Mburu, Mwangi, & Muathe, 2020). Credit risk management has a significant impact on the profitability of commercial banks (Abiola & Olausi, 2014;Mureithi, 2016). Bank management should establish sound credit management based on a moderate credit policy. They should comply with credits standards which encourage the banks to invest in safer assets, such as lower-risk loans or government securities, which may affect bank performance but strengthen their liquidity position and avoid difficulties (Mafumbo, 2020).

The study attempts to answer the main research question: What is the comparative position of loan and advance management of NBL and RBB? Therefore, the paper aims to assess and compare loan and advance management of the two banks operating in Nepal.

The banking sector is largely responsible for collecting household savings in terms of different types of deposits and regulating them into the society by lending them in different sectors of the economy (Shrestha, 1998). Deposits denotes the money kept or held by any bank from their customers especially to accumulate interest. Mainly, there are two types of deposits namely time deposit and demand deposit. The deposit with a fixed interest and term is time deposit. The deposit that can be drawn from the account without providing any prior notice is termed as demand deposit. The greater the amount of deposits, the higher the amount of loan and advances. Total loan to deposit ratio is calculated to describe how successfully the banks are utilizing their deposits on loans and advances for profit generating activities.

Interest is used to describe the cost of using money by borrower. Banks collect money from depositors with low interest thereon and disburse the deposits to borrowers' relatively high interest rate than the deposits. Banks do business with depositor's money. If banks cannot get depositors fund when they want, there might be a defenseless situation in the industry. Public may lose confidence from the bank, which may create problems to run the bank (Akter & Roy, 2017). Interest income is one of the major sources of income for commercial banks. The high volume of interest income on the basis of loan and advance is an indicator of good performance of lending activities.

Banks set loan loss provisions (LLPs) to reflect expected future losses on loans in existing portfolios. Since these future losses cannot be estimated with certainty, bank managers have substantial discretion in setting this provision. In theory, managers exercise this discretion to provide best estimates of their portfolios' expected losses. In practice, however, managers may face substantial incentives to manipulate the loan loss provisions (Anandarajan, Hasan, & Lozano-Vivas, 2005). Nepal Rastra Bank has directed all the commercial banks to create loan loss provision against the doubtful and bad debts. The non-performing loan to total loan and advance ratio helps in minimizing the non-performing loans and helps to control the credit.

There is no global standard to define non-performing loans at the practical level. A non-performing loan (NPL) is a sum of borrowed money upon which the debtor has not made his or her scheduled payments for at least 90 days. NPL is either in default or close to being in default. Once a loan is nonperforming, the chances that it will be repaid in full are considered to be substantially lower. If the debtor starts making payments again on a nonperforming loan, it becomes a re-performing loan, even if the debtor has not caught up on all the missed payments. Non-performing loans comprise substandard loan (loans whose interest or principal payments are longer than three months), doubtful loan (full liquidation of outstanding debts), and unrecoverable or not collectible (Saba, Kouser, & Azeem, 2012). NPL is one of the concrete embodiments of credit risk which banks take. Non-performing loan are those loan that has been default in the payment of interest and principle (Karki, 2019). NPL is a huge puzzle for Chinese commercial banks, so how to enhance risk management to improve assets quality and lower down NPL are of great importance to those banks (Ning-ning, 2007).

NPLs and LLPs maintained by the commercial banks negatively related with the profitability of the business, especially LLPs shown statistical significance to impact on profitability negatively. It is better to take the LLPs and NPLs in the minimum level for maximum profitability of banks. (Islam, 2018). Risk is inherent part of bank's business. Effective risk management is critical to any bank for achieving financial soundness. Credit risk is the bank's risk of loss arising from a borrower who does not make payments as promised. The risk of loss of principal or loss of a financial reward stemming from a borrower's failure to repay a loan or otherwise to meet a contractual obligation is termed as credit risk. Credit risk arises whenever a borrower is expecting to use future cash flows to pay a current debt. Banks are compensated for assuming credit risk by way of interest payments from the borrower or issuer of a debt obligation (Singh, 2013).

Assets are resources and liabilities are source of fund. Bank uses liabilities to buy assets, which earns its income. By using liabilities, such as deposits or borrowings, to finance assets, such as loans to individuals or businesses, or to buy interest earning securities, land and building, plant and equipment etc. the owners of the bank can leverage their bank capital to earn much more than would otherwise be possible using only the bank's capital. Loans and advances is a major part of total assets for the bank. Loan and advance to total assets ratio indicates the volume of loans & advances out of the total assets. A high degree of the ratio indicates that the bank has been able to mobilize its fund through lending.

DATA AND METHODS

The study is based on the Nepal Bank Limited (NBL) and Rastriya Banijya Bank (RBB) of Nepal. NBL was established as First bank of Nepal on Kartik 30, 1994 (November 15, 1937 A.D.) under Nepal Bank Act 1937. The bank was established with an authorized capital of Rs.10 million, issued capital of Rs.2.5 million and paid up capital of Rs.0.842 million. The share held by government and private sector was 60% and 40% respectively. RBB is fully government owned, and was established on Magh 10, 2022 (January 23, 1966) under the RBB

Act. RBB has Nepal's most extensive banking network with over 263 branches. The study used descriptive and analytical research design. Out of 27 commercial banks operating in Nepal, only two commercial banks, NBL and RBB were selected on the basis of judgmental sampling technique. Information was collected from secondary sources including published books and annual audit report of the banks. Then, collected data are checked, reviewed, categorized, tabulated, processed, and analyzed using MS Word, MS -Excel, and SPSS software. While analyzing the data, simple financial and statistical tools like ratios, mean, standard deviation, coefficient of correlation, and coefficient of determination are used. Six hypotheses have been used to measure the relationship of total deposit, loan loss provision, and non-performing loan with loan and advance:

- H01: There is significant relationship between total deposit and loan and advance of NBL.
- H02: There is significant relationship between total deposit and loan and advance of RBB.
- H03: There is significant relationship between loan loss provision and loan and advance of NBL.
- H04: There is significant relationship between loan loss provision and loan and advance of RBB.
- H05: There is significant relationship between non-performing loan and loan and advance of NBL.
- H06: There is significant relationship between non-performing loan and loan and advance of RBB.

RESULTS AND DISCUSSION

Total Deposit, Loan and Advance

Deposits are a stable source of funding for banks. A bank that finds itself with too few deposits to fund loans must rely more heavily on non-deposit sources of funds, whose availability and price are much more sensitive to changing economic or financial conditions (DiSalvo & Johnston, 2017). Total loan and advance to total deposit ratio, commonly known as credit deposit ratio (CD ratio), is the ratio of how much a bank lends out of deposits. Greater CD ratio implies that better utilization of total deposit of banks and higher earnings from the loans and advances with the higher risk. But it should be noted that to high ratio might not be better from its liquidity point of view.

Table 1

Total Loan and Advance to Total Deposit Ratio *(Rs. in Core)*

Fiscal Year	NBL			RBB		
	Total Loans & advance	Total Deposit	Ratio %	Total Loans & advance	Total Deposit	Ratio %
2016/17	7102	9371	75.79	10643	15358	69.30
2017/18	7556	9954	75.90	12087	16933	71.38
2018/19	9242	11720	78.86	14812	19199	77.15
2019/20	10330	14753	72.99	15652	23090	67.79
2020/21	13542	16281	93.17	19597	26384	74.28
Mean			79.34			71.98
S.D.			7.16			3.38
C.V			9.02			4.71

Source: Annual Report of NBL and RBB

Table 1 depicts that the both bank's loan and advances to total deposit ratio are unstable trend. NBL has the highest ratio of 93.17 in the fiscal year 2020/21 and the lowest ratio is 72.99 in the fiscal year 2019/20 but the RBB's highest ratio is 77.15 in the fiscal year 2018/19 and the lowest ratio 67.79 in the fiscal year 2019/20.

The mean ratio of NBL is higher with 79.34% than RBB mean ratio of 71.98%. The lower standard deviation and coefficient of variation of RBB denotes that the bank has more uniformity than the NBL. The result is contrasted with the study end result of the period 2005 to 2010, the average loan and advance to total deposit ratio of NBL was 39.58% while that of RBB was 51.14% (Jha & Hui, 2012).

Interest Income to Loan and Advances

Interest income is one of the major sources of income for commercial banks. The high volume of interest income is an indicator of good performance of lending activities. Table 2 shows the summarized picture of interest income and total loans and advances of NBL and RBB.

Table 2

Total Interest Income to Loans and Advance Ratio *(Rs. in Crore)*

Fiscal Year	NBL			RBB		
	Interest Income	Loan & Advance	Ratio %	Interest Income	Loan & Advance	Ratio %
2016/17	743	7102	10.46	922	10643	8.66
2017/18	923	7556	12.22	1210	12087	10.01

2018/19	1038	9242	11.23	1492	14812	10.07
2019/20	1153	10330	11.16	1716	15652	10.96
2020/21	1189	13542	8.78	1623	19597	8.28
Mean			10.77			9.61
S.D.			1.14			1.09
C.V			10.60			11.32

Source: Annual Report of NBL and RBB

Interest income to loan and advance ratio of NBL ranges from the highest of 12.22 in the fiscal year 2017/18 to the lowest of 8.78 in the fiscal year 2020/21. Similarly, the ratio of RBB is highest of 10.96 in the fiscal year 2019/20 and the lowest of 8.28 in the fiscal year 2020/21 respectively. The mean ratio of NBL is 10.77 which is higher than RBB 9.61. On the basis of coefficient of variation, NBL has more uniformity than RBB since NBL has lesser CV of 10.60% than the RBB of 11.32%.

Loan Loss Provision to Total Loan and Advances Ratio

The provision for loan loss reflects the increasing probability of non-performing loan. Increase in loan loss provision decreases its profit and result to decrease in dividends. But its positive impact is to strengthen the financial conditions of banks by controlling the credit risk and reduced the risks related to deposits. The low ratio indicates the good quality of assets in total volume of loan and advances. High ratio indicates riskier assets in total volume of loan and advances.

Table 3

Loan Loss Provision to Loan and Advance Ratio *(Rs. in Crore)*

Fiscal Year	NBL			RBB		
	Loan Loss Provision	Loan & Advance	Ratio %	Loan Loss Provision	Loan & Advance	Ratio %
2016/17	505	7102	29.67	381	10643	3.58
2017/18	1533	7556	20.29	508	12087	4.20
2018/19	1331	9242	14.40	646	14812	4.36
2019/20	1386	10330	13.42	673	15652	4.31
2020/21	1641	13542	12.12	661	19597	3.37
Mean			17.98			3.96
S.D.			6.48			0.369
C.V			36.03			9.32

Source: Annual Report of NBL and RBB

Table 3 highlights the loan loss provision to total loan and advance ratio of selected commercial banks over the five-year period. The ratio of NBL is highest 29.67 in the fiscal year 2016/17 and lowest 12.12 in the fiscal year 2020/21. Average ratio of NBL is 17.98. Likewise, this ratio of RBB is highest 4.36 in the fiscal year 2018/19 and lowest 3.37 in the fiscal year 2020/21 along with the mean ratio of 3.96. Here, average loan loss provision to total loan ratio NBL is more than RBB and NBL provides huge amount for provision for loan losses. By measuring co-efficient of variation, RBB has more uniformity since it has lesser CV of 9.32 than NBL i.e. 36.03%.

Non-Performing Loans to Total Loan and Advances

Nepal Rastra Bank has directed all the commercial banks to create loan loss provision against the doubtful and bad debts. This ratio helps in minimizing the non-performing loans and helps to control the credit.

Table 4

Non-Performing Loan to Total Loan and Advance Ratio *(Rs. in Crore)*

Fiscal Year	NBL			RBB		
	Non-Performing Loan	Loan & Advance	Ratio %	Non-Performing Loan	Loan & Advance	Ratio %
2016/17	249	7102	3.23	401	10643	3.77
2017/18	255	7556	3.37	574	12087	4.75
2018/19	243	9242	2.61	709	14812	4.79
2019/20	255	10330	2.47	639	15652	4.08
2020/21	278	13542	2.65	602	19597	3.07
Mean			2.75			4.03
S.D.			0.49			0.65
C.V			17.78			16.03

Source: Annual Report of NBL and RBB

Table 4 depicts that the non-performing loan to total loan over the five years study period. The ratio of NBL and RBB ranges the highest of 3.37 in F.Y. 2017/18 and 4.79 in F.Y. 2018/19 and the lower of 2.47 in F.Y 2019/20 and 3.07 in F.Y. 2020/21 respectively. The mean non-performing loan to total loan of NBL and RBB are 2.75 and 4.03 respectively. NBL has the lowest non-performing loan to total loan and advances. Increase in the amount of non-performing loans means mismanagement of loan and deposit of individuals and households (Shrestha, 2018). Thus, NBL is performing good or maintaining their NPLs better than RBB. By measuring coefficient of variation, RBB has more uniformity since its CV 16.03 is lessor than NBL CV of 17.78. The result is not consistent with an empirical study of the Jordanian commercial banks as the study showed that average proportion of non-performing loans to total loans (NPLS) was about 9.88%. The ratio ranged from 0.26% to 31.9%, and the standard deviation was 6.1%. The average ratio of the non-performing loans is relatively high and is close to 10% (Rabab'ah, 2015). But it is consistent with the study of Non-performing loan management of Nepalese commercial bank with reference to Nepal Investment Bank limited and Everest Bank Limited (Adhikari, 2021).

Loans and Advances to Total Assets

Loan and advances is the major part of total assets for the bank. This ratio indicates that the volume of loans and advances out of the total assets. A high degree of the ratio indicates that the bank has been able to mobilize its fund through lending function. However, lending always carries a certain risk of default. Therefore, a high ratio represents low liquidity and low ratio represents low productivity with high degree for safety in terms of liquidity. Table 5 shows total loans and advances and total assets of NBL and RBB.

Table 5

Total Loan and Advance to Total Assets Ratio *(Rs. in Crore)*

Fiscal Year	NBL			RBB		
	Loan & Advance	Total Assets	Ratio %	Loan & Advance	Total Assets	Ratio %
2016/17	7102	13023	54.53	10643	17354	61.33
2017/18	7556	13681	55.23	12087	19733	61.25
2018/19	9242	17151	53.89	14812	22641	65.42
2019/20	10330	19118	54.04	15652	26677	58.67
2020/21	13542	22265	60.82	19597	30999	63.22
Mean			55.70			61.98
S.D.			2.60			2.25
C.V			4.67			3.63

Source: Annual Report of NBL and RBB and

Table 5 presents that the ratio of total loan and advances to total assets in five years. Total loan to total assets ratio of NBL ranges the highest of 60.82% in the fiscal year 2020/21 and the lowest of 53.89 in the fiscal year 2018/19. Similarly, the ratio of RBB is highest of 65.42% in the fiscal year 2018/19 and the lowest of 58.67 in the fiscal year 2019/20 respectively. The mean ratio of NBL is 55.70% which is less than RBB i.e. 61.98.

Correlation between Total Deposit and Loan and Advances

The relationship between the total loan and total deposit is of great significant, as it indicates the direction taken by the total loan with the changes in the volume of total deposit. A bank is unable to provide large volumes of loan if it does not receive adequate and sufficient deposits in a timely basis. The coefficient of correlation between deposits and loan and advance of NBL and RBB are 0.961 and 0.9747 respectively. It shows the positive relationship between these two variables of both banks. The positive relationship shown by their correlation coefficient points out the fact that the changes in each variable are taking place in the same direction, i.e., an increase in total loan is supported by an increase in the total deposit. The result corroborates with the outcome of the study about determinants of lending behavior of commercial banks of Nigeria (Olusanya, Oyebo, & Ohadebere, 2012).

Correlation between Loan Loss Provision and Loan and Advances

The positive relationship shown by correlation coefficient of NBL, points out the fact that an increase in loan and advance has resulted increase in the loan loss provision. On the other hand, the positive correlation of RBB indicates the fact that an increase in loan and advance results increase in loan loss provision.Thus, the relationship between loan and advance and loan loss provision of NBL and of RBB is statistically insignificant which is not corroborate with the result of the study on Loan Management of Nabil and Everest Bank Limited: A Comparative Study (Shrestha, 2018).

Correlation between Non-Performing Loan and Loan and Advances

The relationship between the total loan and total non-performing loans indicates the volume of non-performing loans raised from the total credit granted.

The positive relationship shown by correlation coefficient of NBL denotes the fact that an increase in loan and advance increase in the non-performing loan. On the other hand, the positive correlation of RBB, points out the fact that an increase in loan and advance raise in non-performing loan. The correlation coefficient between loan and advance and total deposit of NBL is significant and RBB is insignificant which is consistent with study entitled Credit risk and commercial bank performance in Nigeria: A panel model approach (Kolapo, Ayeni, & Oke, 2012). The study result is also consistent with the study of non-performing loan management of Nabil Bank and Everest Bank of Nepal (Karki, 2019). It is not consistent with study result of NIBL and EBL as the study showed that there was positive and negative correlation between loan and non-performing loan amount. Both are not moving in the same direction (Adhikari, 2021).

CONCLUSIONS

Loan and advances to total deposit ratio of both banks are inconsistent. The correlation coefficient between loan and advances and total deposit of NBL and RBB are significant and therefore, the null hypotheses are rejected. On the basis of coefficient of variation, NBL has more uniformity than RBB since NBL. Average loan loss provision to total loan ratio NBL is more than RBB and NBL provide huge amount for provision for loan losses. Therefore, NBL has not been able to earn a profit from the point of view of average. The relationship between loan and advance and loan loss provision of NBL and of RBB is statistically significant. It indicates that the RBB cannot manage loan and advance properly. RBB is better mobilizing of fund as loans and advances and it seems quite successful in generating high ratio than NBL. RBB is mobilizing of fund as loans and advances properly. Since the study is related only two commercial banks the findings might not be applicable to all other banks. Therefore, it is recommended for future researchers to widen the scope say, above ten years and to include more banks.

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