Banking System Development in Nepal: A Comparative Analysis

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Abstract

This paper presents the analysis of the structure and major financial highlights of the commercial banking sector in Nepal. As a major component of financial system, the commercial banking sector accounts for more than three fourth of all banking system assets, deposits, loans and investments in Nepal. There is highly asymmetric distribution of assets, deposits, loans and investments within the industry and the market share of public sector banks in terms of overall banking products is still dominant. Despite the satisfactory growth and development of the private sector financial institutions during the nineties, the overall performance of the financial system is undermined due to the problems arising from the two largest public sector banks making huge amount of accumulated loss and non-performing loans (NPLs). The international comparison of the performance of Nepalese banking system with that of selected developed as well as developing economies shows mixed results. Measured in terms of size of financial intermediaries, bank's involvement in the private sector and concentration indices, we find poor indicators of Nepalese banking system compared with some developing and all developed economies. However, the efficiency measures, given by IFS and Fitch's Bankscope data, provide rather ambiguous results showing the comparable ratios of overhead costs and net interest margin to GDP between developed as well as developing economies. The overall analysis shows that the banking sector is/will remain the major source of corporate finance in Nepal. The lack of good and independent corporate governance system and efficient credit monitoring mechanism are the two major reasons for degrading financial conditions of public sector banks (NBL & RBB).

Key words: Corporate finance, Commercial bank, Non-performing loans, Public sector banks, Banking sector reform, Bank-based financial system

I. INTRODUCTION

Nepalese financial system is highly dominated by banking sector. The securities market has very small share in the financial system. Measured in terms of the ratio of total bank assets to market capitalization, the Nepalese financial system falls in the category of bank-based model led by Japan and Germany against the arm' s length securities market-based Anglo-Saxon model. Moreover, a relative measure puts Nepal in the state of underdeveloped bank-based financial system in which both banking sector and securities market indicators rank below the international average.

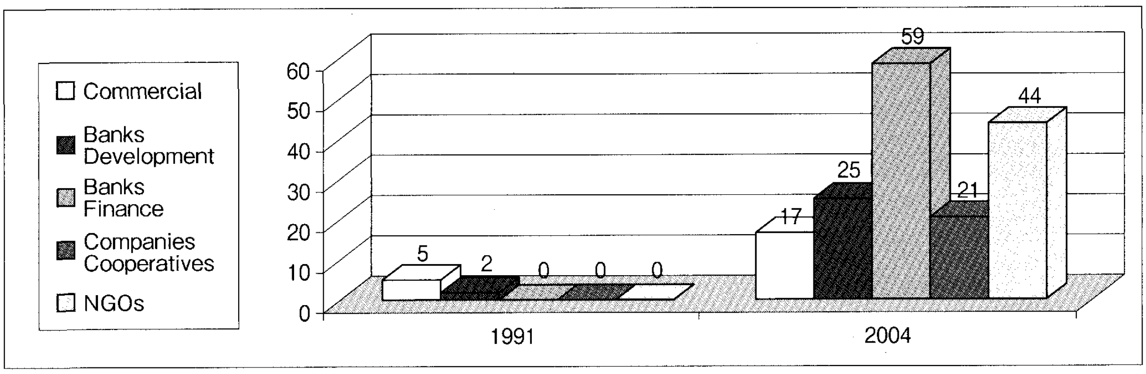
The history of modern banking in Nepal dates back to 1937 with the establishment of Nepal Bank Limited (NBL), the second largest commercial bank, followed by Rastriya Banijya Bank (RBB), the largest commercial bank, in 1966. The establishment of central bank, Nepal Rastra Bank (NRB), in 1956 gradually paved the way for modern banking system in the country. However, the process was rather slow and the system was almost stagnant until the initiation of financial sector liberalization in 1984 that established the first joint venture commercial bank, Nepal Arab Bank (Nabil Bank) as a welcoming step to allow foreign investment in Nepalese banking industry. Until 1991, there were only two public sector the term 'public sector bank' is meant for both RBB & NBL owned fully and partially respectively by the government and three joint venture commercial banks, two public sector development banks, two insurance companies, some postal saving offices and other few financial institutions in Nepal (appendix I).

The financial system underwent a radical change during the nineties. From the relatively closed and regulated environment, the sector was opened up as a part of the efficiency enhancing structural policies to bring about sustainable economic growth. The banking system witnessed a significant change during the decade. New measures were undertaken to induce efficiency and competition. Accounting and provisioning norms, capital adequacy measures, proper risk management measures, etc. were introduced and entry regulations were also eased. The environment was made conductive to the private sector and more market-oriented. Consequently, many new private players entered into the banking sector giving rise to the enhanced efficiency and competitiveness. Despite these significant moves witnessed during the last decade, Nepalese banking sector is still dominated by large public sector banks (although the government owns only 41% of the share of NBL, the term 'public sector bank' is loosely used to mean the government' s involvement in the ownership and operation of this bank) characterized by operational inefficiency, poor financial health and politicization.

The reforms in the banking sector were carried out into two phases. The initial phase consisted of the curative measures, which were brought about for making the banking sector more market-oriented, and impart competition among the players. The second phase consisted of the preventive measures, which were brought about to ensure smooth functioning of the banking system in the long run. The curative measures included the relaxation of interest rate control, reduction of reserve requirements, and lifting of entry barriers. Other measures were prudential norms in terms of following capital adequacy as well as achieving well-defined classification of provisioning standards. Supervisory and regulatory reforms were introduced to ensure transparency and adequate risk management practices were made mandatory. The preventive measure included partial privatization of public sector bank and reduction of government's direct involvement in the banking system. The capital adequacy and several other prudential regulatory measures were made more stringent, and the establishment of Credit Information Bureau and preparations for setting up Asset Management Company are other major reforms in the second phase.

As the consequence of continuous reform initiatives, the Nepalese financial system experienced significant growth and development of financial institutions, services and product innovation. The number of financial intermediaries grew dramatically with the diversified services and products of international standard. Most of the commercial banks, except two public sector banks, have been making relatively good performance despite the stagnant growth of economy since the late 1990s. The expansion of financial institutions has not only contributed to the banking system but also enhanced the scope of securities market. The commercial banks and finance companies are the major listed

Figure 1. Growth of Banks and Financial Institutions



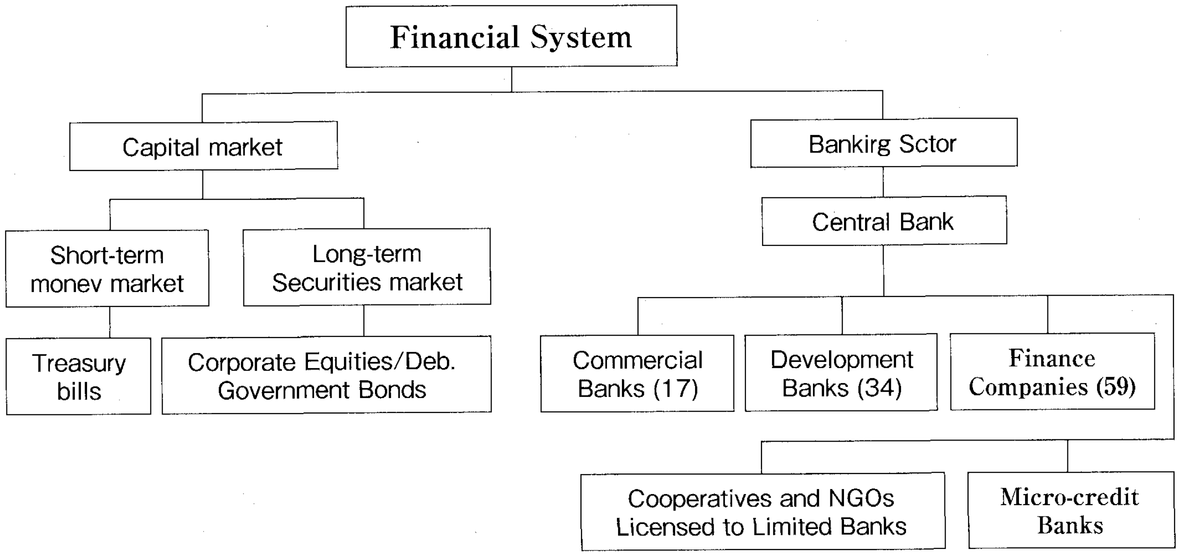
Source- Banking and Financial Statistics (various issues), Nepal Rastra Bank (NRB) companies with significant market share in the stock exchange. Due to the poor performance of manufacturing sector accompanied by the country's weak industrial base and severe politico-economic situation, the investors are often reluctant to invest in the share of manufacturing and other non-financial sector industries. In this backdrop, the banking sector has been playing the dual role for the overall development of the financial system in the country.

1.1. The Structure of Financial System

Financial system can simply be defined as a mechanism that transfers funds from surplus to deficit units. There may be various means or instruments through which funds are channeled and utilized for generating return. The system, as a whole, consists of the legal and institutional structure, financial instruments and individuals. It performs the functions of mobilizing savings, allocating resources, exerting corporate control, facilitating risk management and easing trades and contracts. More concisely, banking sector and the securities market are the two major constituents of the financial system. These both components are subject to facilitate the needy ones by providing long as well as short-term investment funds. The choice between these two methods of financing decision depends, among other things, on the risk and return factors, level of socio-economic condition and the government policy designation.

Obviously, the bank loan is the main source of corporate finance in Nepal. The share of bank credit as percentage of GDP increased from 29 percent in 1990 to 50 percent in 2003. This shows an increasing role of banking sector in supplying the growing demand of domestic credit in the economy. Similarly, the bank deposits as percentage of GDP has been rising continuously over the period implying that the bank deposit has been/will be the largest component of household financial assets. Moreover, the market capitalization as percentage of GDP is also increasing, which indicates that the size of securities market is growing gradually over time. However, the share of securities market in the overall financial system is very small and still not remarkably significant. The following chart simply exhibits the anatomy of Nepalese financial system.

The major features of Nepalese financial system are summarized as follows: First, the Nepalese financial system can be leveled as the bank-centered system however, international comparison shows that Nepal has underdeveloped financial system, which

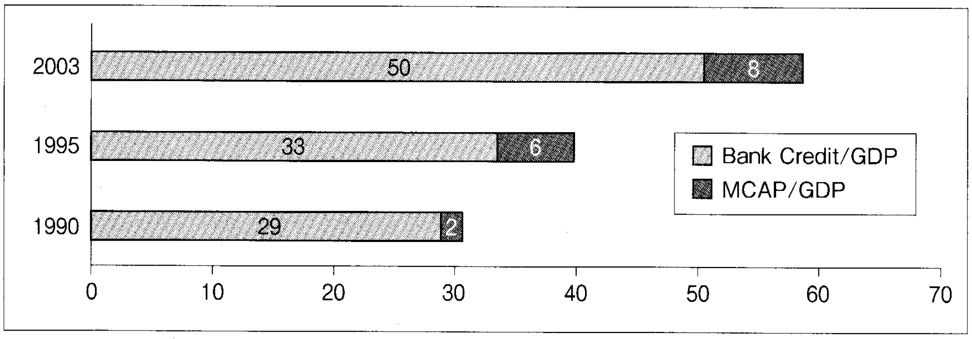


is not meaningfully comparable to bank-based (Japan-German) vs. securities market-based (Anglo-US) models. Second, the securities market is in the infant stage of development and hence the bank loans are the major source of corporate finance. Followed by the universal banking model, the commercial banks are the major players in the financial system. Third, the securities market, particularly the equities market, is largely confined to the banking sector. The manufacturing sector has relatively small share in the market. The major (top ranking) industries listed in the stock exchange are either banks or finance companies with relatively small number of other non-financial sector industries.

Fourth, due to the lack of knowledge and sufficient information about securities business, the general people, except few professionals, are often reluctant to invest in the securities market and hold their financial assets in the form of bank deposits. Similarly, due to the lack of relatively less risky market instruments such as, corporate debentures than highly volatile equities investment, the general people are compelled to allocate their limited earning in the form of bank deposits yielding low return. Also the risk aversion behavior of the people has a significant influence on it. These factors have limited the scope of securities market in the country. Fifth, the banking system is highly dominated, in all aspects, by the two largest public sector banks (NBL and RBB), which have been technically insolvent and currently operating with severe financial health as well as managerial distress. Moreover, these banks are highly unequipped, poorly managed and triggered by political interference. The private sector banks, on the other hand, have shown good performance with diversified services and products of international standard. Nevertheless, the overall banking system indicators are quite poor due to the large market share of problem-led public sector banks. Moreover, there is high concentration of assets, deposits, loans and investments with small number of banks.

Sixth, there exists large presence of informal financial transactions, particularly in the rural areas, in Nepal. Though it is difficult to quantify the amount, it is true that a large fraction of rural people, especially, small and poor farmers and shopkeepers, make use of such loans because of their inability to meet administrative and legal requirements for bank loans and also due to the lack of easy banking access in their locality. Finally, the lack of uniform accounting and reporting system, poor disclosure and transparency mechanism and weak corporate governance system are other salient features of Nepalese financial system.

Figure 2. Bank Credit vs. Market Capitalization to GDP



Source- Quarterly Economic Bulletin Mid-July 2004 NRB/ Economic Survey, HMG/N.

To sum up, Nepal has bank-based financial system. Although the history of Nepalese banking sector dates back to 1937, it was almost stagnant until the initiation of financial system liberalization in the mid-1980s. The reforms in the banking sector were carried out into two phases. The first phase consisted of the curative measures, which were brought about by making the banking sector more market-oriented and impart competition among them. The second phase consisted of the preventive measures that aimed to ensure long-run growth and development of banking system. As the consequence of various reform initiatives, the banking sector witnessed a quantum jump during the last decade. Nevertheless, the overall banking system indicators are rather poor due to the large market share of problem-led public sector banks. The historical and current analysis indicates that the bank credits remain/will remain the major source of corporate finance and the bank deposits as the largest component of household financial assets in Nepal. There is limited choice of corporate finance from bank to securities market in Nepal. Due to the inadequate securities market infrastructure and small size of industrial undertakings within a small number of public limited companies, the Nepalese financial system is highly dominated by banking sector and is likely to follow the same pattern in the future until the market infrastructures are developed and corporate sector earns sufficient credibility (Pokhrel, 2005).

II. THE STRUCTURE OF COMMERCIAL BANKING IN NEPAL

Although the securities market is still passing through the infant stage of development, the banking sector in Nepal has relatively longer historical foundation, established institutional settings and better growth and development trend. The banking system is composed of commercial banks, development banks, finance companies, micro-credit banks, co-operatives and NGOs licensed to carry out limited banking activities. This study, however, does not take into account other components except commercial banking sector. Due to the significantly high market share of commercial banks, the study mainly concentrates in the structure, performance and major problems of commercial banking sector shading lights on the two largest public sector commercial banks.

The commercial banking sector is the major and largest component of Nepalese financial system. It is not only the main constituent of banking system but also a major player in the securities market. Due to weak infrastructure and poor performance of manufacturing and service industries, the securities market activities are largely confined to the banking industries that have been showing relatively better performance than other non-banking sector industries since the early 1990s.

The commercial banking sector alone accounts for 80 percent of total assets, 72 percent of total loans and advances, 88 percent of total investments and 81 percent of total deposits of the overall banking system as of 2003. The shares of these major banking activities were much higher in the past, except the share of investment, as shown in the table 2.1. The table gives an impression that the commercial banks are the major players in the Nepalese banking industry. The summary of sources and uses of funds of commercial banks are given in the appendix (appendix II).

Table 2.1. Financial System at a Glance (Rs. in million)

	1998	1999	2000	2001	2002	2003
Deposits	109553.7	1367107.9	165981.9	197325.6	225187.4	251742.3
Commercial Banks %	94	93	93	92	82	81
Finance Companies %	6	6	6	6	6	7
Development Banks* %	0	0	0	1	11	11
Co-operatives %	0	1	1	1	1	1
Investment	13094.5	15972.4	19488.5	27398.5	39279.7	51457.9
Commercial Banks %	83	89	92	93	87	88
Finance Companies %	13	8	6	5	4	5
Development Banks* %	3	2	1	2	8	7
Co-operatives %	0	0	1	1	0	0
Loans and Advances	74875.6	90124.4	106996	124048.9	155138.5	173914.8
Commercial Banks %	92	91	90	88	73	72
Finance Companies %	7	8	8	9	8	8
Development Banks* %	0	1	1	2	19	19
Co-operatives %	1	1	1	1	1	1
Total Assets/Liabilities	155444.8	185555.9	225553.5	253946.2	335440.6	318598.4
Commercial Banks %	94	93	93	92	82	80
Finance Companies %	5	6	6	6	6	6
Development Banks* %	1	1	1	2	12	13
Co-operatives %	0	0	0	1	1	1

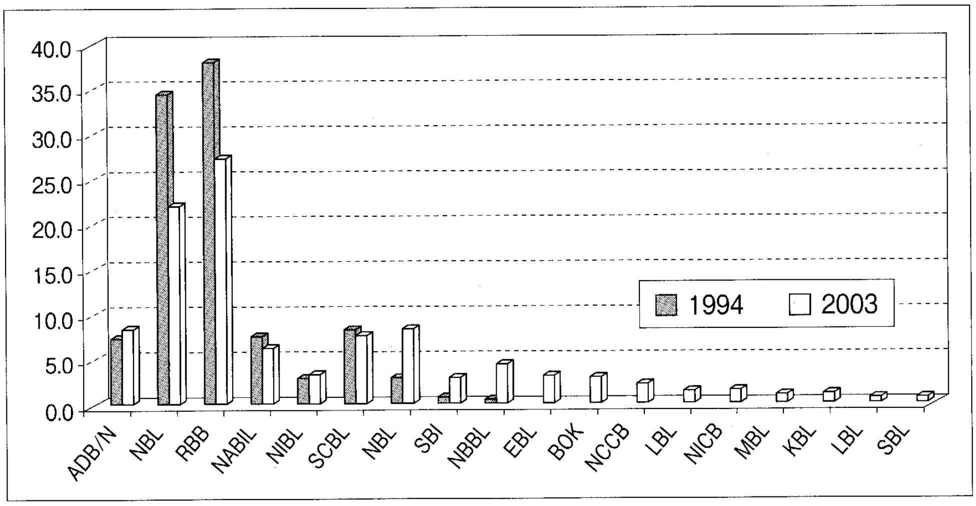
* Including micro-credit development bank. Up to mid-July 2000, NIDC and ADB/N are excluded, in mid-July 2001; NIDC is excluded, Source- Banking and Financial Statistics, no. 42, January 2004, NRB.

2.1. Assets

The assets of the commercial banks grew at an annual average rate of 21 percent over the period from 1990 to 2003. The share of assets within the commercial banks is highly concentrated with two public sector banks. Of the total assets of the commercial banks (including the assets of the branches of Agricultural Development Bank performing commercial banking activities), these two public banks (combined) account for about 49 percent in 2003, which was 72 percent in 1994.

Although the proportionate share of these two banks is declining over the last few years, the concentration of total banking assets is still high as shown in the figure3. Of the total 17 commercial banks, 9 were established as the joint venture but currently, the number has declined to 6 when 3 of them have recently sold their share ownership to the Nepalese investors.

Figure 3. Share of Assets (commercial banks)



Source- Banking and Financial Statistics, no. 42, NRB.

The joint venture banks hold 31 percent of total commercial banking assets in 2003. Three large banks, Himalayan Bank, Standard Chartered Bank and Nabil Bank, dominate the joint venture group. These banks hold 21.4 percent of total commercial bank assets that account for about 69 percent of the total assets of the joint venture banks in 2003. Despite the rapid growth in the number of domestic private banks over the last few years, the assets share of these banks is still very small (12.5 percent in 2003) as shown in the figure 3. It has been clear from the statistics that that the assets are asymmetrically distributed in the banking system.

2.2. Deposits

The commercial banks hold 81 percent of total deposits of the banking system in 2003 that came down from 94 percent in 1998. Of the total commercial bank deposits (including ADB/N) of Rs. 203.8 billion, NBL and RBB hold 36.3 percent in 2003, which declined substantially from 65.2 percent in 1994. This share amounts to 48 percent in 2003 including the total deposits of another public bank, Agricultural Development Bank (ADB/N). The combined share of total deposits of the joint venture banks accounts for about 38 percent in 2003, an increase from 33 percent in 1996. The share of other privately owned domestic commercial banks is about 15 percent in 2003. Himalayan Bank, Standard Chartered Bank and Nabil Bank, the 'three good name' joint venture banks, hold a combined share of 26 percent of total commercial bank deposits. Of the total deposits, the saving deposits constitute the largest proportion, 48 percent, in 2003 followed by fixed (31%) and current (14%) deposits.

Figure 4 (a). Public Bank Deposit mid-Jan 2004

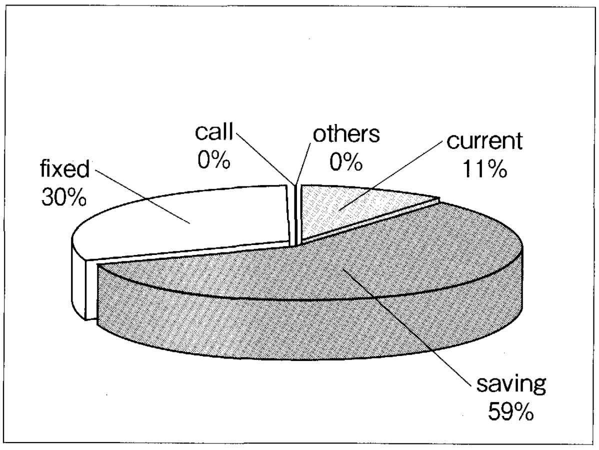
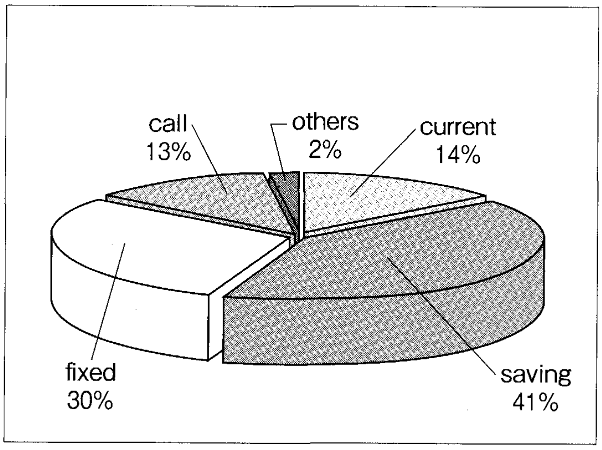


Figure 4 (b). Public Bank Deposit mid-Jan 2004



Source- Banking and Financial Statistics, no. 42, NRB.

2.3. Loans and Advances

Of the total banking system loans and advances of Rs. 173.9 billion, the commercial banks hold 72 percent in 2003, which stood at 92 percent in 1998. The share of loans and advances by the public sector bank has substantially declined to 38.2 percent in 2003 from 65.4 percent in 1994. Of the total loans and advances of Rs. 124.5 billion, the private sector accounts for 97 percent in 2003, which was 93 percent in 1996.

The loans and advances to the government enterprises are declining whereas the private sector loans and advances are gradually increasing. The share of joint venture and domestic private banks has been increasing since the late 1990s. The joint venture banks hold 38 percent share whereas the domestic private banks jointly hold about 17 percent of total loans and advances. Although the private sector banks are increasing their market share of loans and advances, the public sector banks still hold a significant proportion. The loans and advances as percentage of total deposits grew from 52.3 percent in 1994 to 61.1 percent in 2003. The ratio of loans and advances to total deposits shows poor intermediation in the banking system, however, the trend is improving. The loans and advances account for 41 percent of total uses of funds of the commercial banks in 2003.

2.4. Investment

The investment of commercial banks accounts for 88 percent of total banking system investment in 2003. The investments comprise 15 percent of total uses of funds in 2003 that stood at 20 percent in 1994. Of the total investments of Rs. 45.4 billion in 2003, RBB and NBL hold 35 percent share that sharply came down from 74 percent in 1994. Due to the increasing presence of joint venture banks, public banks' share of the total commercial bank investment substantially declined over the period 1994-2003.

Of the total investment, the joint venture banks account for 51 percent while the share of domestic public banks remains at 14 percent in 2003. The corresponding share was 30 percent and 0 percent respectively in 1994. The Standard Chartered Bank, the largest joint venture bank, alone holds about 23 percent of total commercial bank investments in 2003. The investment in the government securities averaged on 89 percent of total investment over the period 1994-2003. The investment on the share, debenture and NRB bond stood at an annual average of 11 percent over the period. This shows that commercial banks make largest proportion of their investment in government securities. The investment on the share and debenture of corporations are negligible. The concerns over the risk and the lack of enough investment opportunities in securities market are the major reasons for excessive concentration of commercial banks' investment on government securities.

2.5. Ownership Structure

Of the total 17 commercial banks, RBB is fully owned by the government. The NBL, the second largest commercial bank, was established as a joint contribution of government and the private sector with the share ownership of 51 percent and 49 percent respectively. In the process of financial sector liberalization, the government has sold its 10 percent share ownership to the general public. Thus, the majority share (59 percent) of bank is now owned by the private sector leaving 41 percent to the government. However, the government still has significant influence in the management and operation of this bank. There were 9 joint venture banks but three of them have sold the share their foreign owners to the Nepalese investors. Standard Chartered Bank Nepal Limited, Himalayan Bank Limited and Nabil Bank Limited are the three well performing joint venture banks with highly professoalized management, quality-banking services and advanced technology. Remaining 9 banks are fully owned by private Nepalese investors, general public, various government and privately owned institutions. The existing joint venture banks with their paid up capital, equity ownership by the foreign banks are listed in the following table.

Table 2.2. Joint Venture Commercial Banks

S.N.	Bank	Paid-up Capital (Rs.in million) Mid-July 2003	Foreign Share (%)	Foreign Shareholders
1	Himalayan Bank Limited	429.0	20	Habib Bank Ltd., Pakistan
2	Everest Bank Limited	455.0	20	Punjab National Bank, India
3	Nepal SBI Bank Limited	425.2	50	State Bank of India, India
4	Nabil Bank Limited	491.7	50	National Bank Ltd., Bangladesh
5	Standard Chartered Bank Nepal Ltd.	339.5	75	Standard Chartered Bank, Australia
6	Nepal Bangladesh Bank Limited	359.9	50	IFIC Bank, Bangladesh

Source- Compiled from banks' reports to NRB.

2.6. Branch Network

Until mid-January 2004, there were 375 commercial bank branches throughout the country. Including the branches of ADB/N, performing commercial banking activities, the total number comes at 423. The branch network is highly concentrated with the two public sector commercial banks and ADB/N. The two public sector banks hold 59 percent of total branch network of commercial banks followed by ADB/N with 11-percentage share. Of the total branches, 201 are located in the Central Development Region, 86 in Eastern Region, 80 in Western, 30 in Mid-Western and 27 in Far-Western Development Region. About 21 percent of total branches are located in Kathmandu Valley where the most banking activities take place. In the recent years, increasing security threat has severely affected banking sector. The rural branches in many places of the country are closing down their operation due to security problem and downsizing of economic activities. There were 445 commercial bank branches throughout the country until mid-July 2000. Including the branches of ADB/N operating commercial banking activities, the number was 484. Over the period 2000-2003, there has been a substantial reduction in the branch network of commercial banks as shown in the following table.

Table 2.3. Commercial Bank Branches

Development Region	Eastern	Central	Western	Mid-Western	Far-Western	Total
	Mid-July 2000					
Commercial Banks	104	195	79	34	33	445
Agricultural Devt. Bank	6	24	6	2	1	39
Total	110	219	85	36	34	484
	Mid-January 2004					
Commercial Banks	79	171	73	27	25	375
Agricultural Devt. Bank	7	30	7	2	2	48
Total	86	201	80	29	27	423

Source- Banking and Financial statistics, Various Issues, NRB.

To sum up, the commercial banking sector is the largest component of Nepalese banking system. This sector alone accounts for 80 percent of total assets, 72 percent of total loans and advances, 88 percent of total investments and 81 percent of total deposits of the overall banking system (as of 2003). The distribution of assets, deposits, loans and investments is asymmetric. The private banks, led by the joint venture banks, have been increasing their market shares of all types of banking products in the recent years. Of the total 17 commercial banks, one is fully owned and operated by the government; one is semi-public with 41 percent of share owned by the state, 6 are jointly established banks with varying share ownership by foreign partners and remaining 9 banks are owned by Nepalese investors, institutions and general public. Due to the increasing security problems and the resultant economic slowdown, many commercial bank branches have been/are being closed.

III. THE PUBLIC SECTOR COMMERCIAL BANKS

3.1. Nepal Bank Limited (NBL)

The history of modern banking began in Nepal with the establishment of Nepal Bank Limited (NBL) in 1937 under 'Nepal Bank Act 1937' . The bank was established as the joint contribution of government and private sector with the share ownership of 51 and 49 percent respectively. With the government divestment of 10 percent of its share ownership in 1998, the majority share of the bank is now owned by the private sector.

However, the government has significant influence in its management and operation. The bank holds significant amount of shares of various financial institutions, such as Standard Chartered Bank Nepal Limited, Nepal Insurance Company, Nepal Oil Corporation, NIDC, etc. The bank had initial authorized capital of Rs. 10 million and paid-up capital of Rs. 842 thousand, which was increased to 2.5 million in 1956. Until 1956, after 19 years of its operation, the bank had only 12 branches. By 1990, the bank was being operated by 8,721 staff and 235 branches throughout the country, which were reduced to 6,000 and 211 respectively in 1998. Until mid-July 2003, the bank had 5,242 staff and 116 branches (Nepal Rastra Bank).

Prior to 1937, the monetary transactions were monopolized by private dealers. The establishment of NBL significantly contributed to industry, trade and agriculture development through the mobilization of deposits to loans and investments. Until the establishment of Nepal Rastra Bank in 1956, NBL played the dual role of commercial as well as central banking in the country. It was serving as the banker to the government in the absence of central bank. This was the only commercial bank in the country until the next fully government owned commercial bank (RBB) was set up in 1966.

With the paid-up capital of Rs. 1,064.3 million, the bank currently owns the total assets of Rs. 63,436.2 million, which represents 20 percent of total commercial banking assets and 16 percent of whole banking system assets as of mid-January 2004. Of the total assets, loans and advances comprise the largest share (30 percent as of mid-Jan 2004) followed by investments (21 percent). The average investment in the government securities accounts for 91 percent of the total investment over the period 1994-2003. The annual growth rate of assets has shown high fluctuations ranging from minus 3 percent in 1995 to 30 percent in 1998. Over the period 1994-2003, the assets grew at an annual average rate of 12 percent. Similarly, the deposits, loans & advances, and investment grew at an annual average rate of 8 percent, 10 percent and 57 percent respectively over the period 1994-2003.

The saving deposits represent the largest share of total deposits followed by fixed and current deposits. The share of saving deposits continued to exceed fixed deposits, except in 1994 and 1998, and stood at more than 50 percent since 2000 and reached to 62 percent in mid-January 2004. The investment in the NRB bond accounted for 34 and 12 percent in 1994 and 1995 respectively and since 1998, the bank allocated almost all

(99 percent) of its investment in government securities. Of the total loans and advances, the private sector loans account for more than 90 percent between 1994 and 1997 and the share increased to more than 95 percent since 1998. This shows the bank's increasing involvement in providing services to private sector. However, the bank's loans to the public enterprises have remained constant except some marginal increase in 1997, 2000 and 2003.

Extending from its 12 branches in 1956, the bank had set up 211 branches and around 6000 staff at the end of 1998 (World Bank, 2002). Due to the increasing security problems, many rural branches are closed down and a number of other branches are in the position to close their operation if the situation does not improve. Until mid-January 2004, there were 116 branches of NBL that account for 31 percent of total (375) commercial bank branches throughout the country. The branch network has been drastically reduced during the last few years due mainly to the degrading security situation and economic slowdown in the country, especially in the remote rural areas. The summary of assets and liabilities of Nepal Bank Limited over the period 1994-2004 is given in the appendix (Appendix III).

The share of deposits in the sources of fund has been declining since 2001. The credit-deposit ratio stood highest at 84 percent in 1997 and gradually declined to 53 percent in 2004. This phenomenon shows the poor intermediary role of the bank. The NBL deposits account for 9 percent of GDP, on average, over the period 1994-2004 while the share of whole commercial bank deposit to GDP stands at 36 percent over the same period. This shows that the NBL holds a significant amount of banking system deposits in the country. Similarly, the total assets of NBL accounts for 12 percent of GDP compared with 52 percent for all commercial bank assets to GDP over the period 1994-2004. The asset-GDP ratio is increasing marginally over the period under review. The growth rate of loans and advances has become negative since 2001. Similarly the growth of assets sharply declined since 2002 and turned negative in the mid-January 2004. The growth rate of investment shows high fluctuations since 1998. The major indicators (ratios) and their growth trend are depicted in the following table.

Table 3.1. Some major Indicators (Ratios) of Nepal Bank Limited, percent

FY (mid-July)	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004*
Credit-Deposit	51	63	75	84	69	68	64	62	62	55	53
Investment-Deposits	38	23	10	3	16	15	15	19	21	34	37
Capital-Assets	2	3	3	3	2	2	2	2	2	2	2
Deposits-Assets	71	77	78	74	74	75	77	70	53	52	56
Deposits-GDP	**9**	**9**	**8**	**8**	**9**	**10**	**9**	**9**	**8**	**8**	**7**
Assets-GDP	**13**	**11**	**10**	**10**	**13**	**13**	**12**	**12**	**15**	**15**	**13**
Total Bank Assets-GDP**	**37**	**38**	**41**	**42**	**48**	**51**	**56**	**62**	**64**	**67**	**64**
Growth Rate of:											
Investment	-	-38	-53	-66	556	14	7	24	6	65	12
Loans and Adv.	-	31	25	22	8	15	2	-4	-5	-8	-2
Deposits	-	5	6	8	31	18	8	0	-4	2	3
Assets	-	-3	6	14	30	17	4	10	25	4	-4

Source-Calculated from various NRB Publications, *as of mid-January, ** total commercial banks

3.2. Rastriya Banijya Bank

Rastriya Banijya Bank (RBB), established in 1966, is the largest commercial bank fully owned by government. The bank had initial authorized capital of Rs. 10 million and paid up capital of Rs. 2.5 million. Currently, it has the paid-up capital of Rs. 1172. 3 million (as of mid-January 2004). The bank owns the largest amount of assets that accounts for 27 percent of total commercial bank assets (as of mid-July 2003), which was about 38 percent in 1994. This bank alone holds 21 percent of total banking system assets (as of mid-January 2004). Through the ongoing restructuring process, the number of branches has been reduced from more than two hundred to around 116 nationwide and the headcount is now being reduced from 5310 as of mid-July 2003 to a figure close to 3200 (NRB, 2004). As of May 2004, the total employees of the bank were 3800 (RBB, 2004). Of the total assets of the banks, loans and advances accounts for the largest share (41percent), on average, over the period 1994-2004 followed by liquid funds (16 percent) and interest accrued (13 percent). The assets grew at an annual average rate of 13 percent over the period 1994-2003. Similarly, deposits, loans & advances and investment grew at an annual average rate of 11 percent, 12 percent and 7 percent respectively over the same period.

The total deposit of RBB accounts for 9 percent of GDP, on average, over the period 1994-2004. Of the total deposits, the fixed deposits outstripped saving and current deposits until 2000 and thereafter the composition altered, led by the saving deposits (from 46 percent in 2001 to 57 percent in mid-January 2004). Almost all of the bank's investment (more than 96 percent) has been made on the government securities. The loans to private sector accounts for more than 96 percent of total loans and advances implying the bank's significant involvement in providing credit to the private sector.

The credit-deposits ratio stood highest at 86 percent in 1996 and declined steadily thereafter until it reached to 70 percent in mid-January 2004. The assets of RBB alone account for 16.5 percent of GDP, on average, over the period 1994-2003. This ratio for whole commercial banking system stands, on average, at 51 percent over the same period. The credit-deposit ratio reached at the highest level in 1996 and gradually declined since then. The ratio has been more stable ranging between 70 to 73 percent over the last few years. RBB has higher credit-deposit ratio than that of NBL showing that the former has better intermediation function than the later. The average ratio of credit plus investment to deposits is about 90 percent whereas this ratio of NBL stands at 85 percent on average over the period 1994-2003.

Table 3.2. Major Indicators of Rastriya Banijya Bank, Percent

FY (mid-July)	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004*
Credit-Deposit	66	75	89	86	83	79	76	70	73	72	70
Investment-Deposits	22	15	10	7	9	8	11	14	11	11	15
Capital-Assets	4	4	3	3	3	3	2	2	2	2	2
Deposits-Assets	59	59	53	52	54	62	59	55	51	48	47
Deposits-GDP	**8**	**9**	**8**	**8**	**9**	**10**	**10**	**10**	**9**	**9**	**8**
Assets-GDP	**14**	**15**	**16**	**15**	**17**	**16**	**17**	**18**	**18**	**18**	**17**
Total Commercial Bank Assets-GDP	**37**	**38**	**41**	**42**	**48**	**51**	**56**	**62**	**64**	**67**	**64**
Growth Rate of:											
Investment	Na	-23	-29	-27	64	17	56	30	-26	1	39
Loans and Adv.	Na	30	31	3	18	18	11	-2	0	-1	-2
Deposits	Na	15	10	6	22	24	15	5	-4	1	1
Assets	Na	16	21	9	18	7	21	13	3	8	3

Source- Compiled and calculated from various NRB publications, * mid-January.

3.3. Structure of Loans and Branch Network of NBL and RBB

The loans to production sector accounts for the largest share of total loans followed by the share of wholesalers and retailers as shown in the table 3.3. The statistics clearly show that the loan share of NBL to the production and service sector is much higher than that of RBB. On the other hand, RBB' s loans to the wholesalers and retailers are much higher than that of NBL. Similarly, RBB' s loans share to the agriculture sector is higher than that of NBL.

Table 3.3. Sector wise Loans of Public Sector Banks, NBL & RBB (Rs.in million)

	Mid-July 2004				Mid-July 2003			
Sectors	NBL	%	RBB	%	NBL	%	RBB	%
Agriculture	884	5	1,756	7	697	4	1,679	6
Mining	29	0	24	0	48	0	61	0
Productions	6,070	34	6,566	26	6,708	35	6,935	25
Constructions	331	2	351	1	339	2	353	1
Metal Prodn. Machinery and Electrical tools	198	1	130	1	154	1	136	0
Transportation equipment production	87	0	432	2	49	0	512	2
Transportation communications & public services	389	2	1,090	4	384	2	1,212	4
Wholesaler and retailers	3,751	21	10,271	41	4,079	21	9,060	32
Finance, Insurance and Fixed assets	418	2	78	0	487	3	478	2
Service Industries	2,265	13	1,770	7	2,574	13	1,855	7
Consumable Loans	2,487	14	754	3	1,126	6	1,027	4
Local Government	0	0	0	0	0	0	0	0
Others	1,055	6	1,913	8	2,621	14	4,951	18
Total	17,965	100	25,133	100	19,266	100	28,259	100

Source- Bank and Financial Statistics, no .41 & 43, NRB.

The public sector banks are the major sources of agricultural loan among the commercial banks. The RBB alone extended 45 and 36 percent of total commercial bank loans to agriculture in 2003 and 2004 respectively. Similarly, the corresponding share of NBL accounts for 19 and 18 percent in the same years respectively. These banks are also the largest sources of consumer loans that stood at 65 and 74 percent of total loans extended in this sector in 2003 and 2004 respectively. Moreover, the loan share of these banks in wholesaler and retailer, service, finance, insurance and fixed assets sector is significant. The statistics (table 3.4) clearly show that these two banks are the major sources of loans and advances especially in agriculture and consumer loan sector. However, the share of these banks in the total commercial bank loans and advances declined from 38 percent in 2003 to 31 percent in 2004.

The data on the securities wise loans and advances of commercial banks show that the fixed assets are the largest securities bases for RBB as well for whole commercial banking sector in 2003 and 2004. However, for NBL, the current assets stand for the

Table 3.4. Sector wise Loan Share of Public Sector Banks (NBL and RBB)

Sectors	Mid-July 2003			Mid-July 2004		
	All Banks (Rs.in million)	% Share of NBL	% Share of RBB	All Banks (Rs.in million)	% Share of NBL	% Share of RBB
Agriculture	3,730	19	45	4,902	18	36
Mining	394	12	15	337	9	7
Productions	41,671	16	17	47,369	13	14
Constructions	2,789	12	13	4,987	7	7
Metal Prodn., Machinery and Electrical tools	1,429	11	10	1,451	14	9
Transportation equipment production and fitting	1,370	4	37	2,777	3	16
Transportation communications & public services	6,169	6	20	7,964	5	14
Wholesaler and retailers	25,423	16	36	31,729	12	32
Finance, Insurance and Fixed assets	4,117	12	12	4,857	9	2
Service Industries	12,151	21	15	14,217	16	12
Consumable Loans	3,323	34	31	4,400	57	17
Local Government	2	0	0	2	0	0
Others	21,954	12	23	12,372	9	15
Total	124,522	15	23	137,361	13	18

Source- Bank and Financial Statistics, no.41 & 43, NRB.

largest securities source in the same years. The table 3.5 shows that RBB extended about 77 % and 70 % of total loans based on the securities of fixed assets in 2003 and 2004 respectively. NBL, on the other hand, extended 29 and 28 percent of its total loans based on the securities of current assets in the same years respectively. The table shows that the assets guarantee represents the largest securities for loans in the overall commercial banking system. However, there is high difference between RBB and NBL in the share of loans extended on the basis of fixed vs. current assets as the securities.

Two public sector banks (RBB & NBL) have the largest number of branch network throughout the country. The branch network of these two banks accounts for 55 percent of total commercial bank branches in 2004. A majority of rural branches of RBB and NBL is involved in extending priority sector lending (the present mandatory rate at not less than 12% of total outstanding loans and advances) which is an important element for meeting the prioritized development financing needs and also extending the reach of the formal financial structure especially in the rural areas.

Table 3.5. Securities-wise Loans & Advances of Commercial Banks (as % of total)

Types of Securities	Mid-July 2004 NBL	RBB	Private Banks	All Commercial Banks	Mid-July 2003 NBL	RBB	Private Banks	All Commercial Banks
Gold/Silver	3.8	2.1	0.1	1.0	4.1	2.7	1.1	2
Government Securities	8.8	0.1	3.2	3.3	0.5	0.1	2.4	2
Non-govt. Securities	0.0	0.0	1.1	0.7	0.0	0.0	1.2	1
Fixed A/C Receipt	1.2	0.8	2.5	2.0	1.3	0.8	2.8	2
Asset Guarantee								
Fixed assets	24.7	76.8	58.4	57.3	25.1	69.8	53.0	52
Current Assets	29.3	4.8	19.9	18.3	27.6	3.4	21.6	18
On Bills Guarantee	5.3	12.9	5.7	7.1	7.3	11.0	6.5	8
Guarantee								
Govt.	2.5	0.0	0.1	0.5	3.8	0.0	0.0	1
Institutional	0.8	0.0	2.7	1.9	0.7	0.0	3.1	2
Personal	1.2	0.0	0.7	0.6	1.6	0.0	1.0	1
Group	0.4	0.4	0.0	0.1	0.4	0.3	0.1	0
Others	0.5	0.0	1.9	1.3	0.4	0.0	2.6	2
Credit Card	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0
Earthquake Victim Loan	0.2	0.2	0.0	0.1	0.2	0.2	0.0	0
Others	21.1	1.8	3.8	5.8	27.1	11.5	4.7	10

Source- Bank and Financial Statistics, no.41&43, NRB.

Table 3.6. Branch Network of NBL and RBB (as of July 2004)

Regions (Districts)	Eastern (16 districts)	Central (19 districts)	Western (16 districts)	Mid-Western (15 districts)	Far-Western (9 districts)	Total (75 districts)
Population *	5,344,476	8,031,629	4,571,013	3,012,975	2,191,330	23,151,423
Commercial Banks	79	171	73	27	25	375
Agricultural Devt. Bank	7	30	7	2	2	48
All Banks Total	**86**	**201**	**80**	**29**	**27**	**423**
Branch Per Capita (per 1000 pop.)	0.02	0.03	0.02	0.01	0.01	0.02
Nepal Bank Limited	29	51	19	11	6	116
Rastriya Banijya Bank	31	43	19	12	12	117
NBL & RBB Total	60	94	38	23	18	233
Share of NBL & RBB	**70**	**47**	**48**	**79**	**67**	**55**

Source- Bank and Financial Statistics, 43. July 2004, NRB, *Based on 2001 Census, CBS/HMGN

Of the total 130 branches maintaining the government account (as of 2001), 120 or 92% of the total, belong to these banks. Sixty-six branches of these 2 banks, or 88% of the total, carry out government's budgetary expenditure release operations in the same number of districts. These branches made all the receipts and payments on behalf of the government offices and government projects along with preparing the necessary accounts of transactions (Nepal Rastra Bank, 2003). This shows that the NBL and RBB play significant role not only in commercial banking but also in the government budgetary operations.

3.4. Major Problems of Public Sector Banks (NBL and RBB)

Although NBL and RBB have been playing significant role in the financial system, the degrading financial as well as managerial situation of these banks resulted from the past mistakes have brought them in the serious crisis. Both banks exhibit serious problems of poor management, weak governance and fragile financial health, leading to a high level of non-performing assets and accumulated losses. The Commercial Banks Problem Analysis and Strategy Study (CBPASS) undertaken in 1988 had given early signals urging the authorities to take necessary steps for loan recovery mechanism. The recommendation of the CBPASS started to be implemented since 1989, comprising a number of reform agenda including capital injection. The reform measures in the first phase encompassed recapitalization, loan loss provisioning, and repayment of government-guaranteed loans to the public enterprises. A supplementary budget of Rs. 3.45 billion was announced to implement this program and accordingly, the proposed capital was injected in these banks (Nepal Rastra Bank, 2003). In the second phase, the restructuring of these banks was envisaged in terms of credit administration, asset and liability management, improvement of management information, office administration and reduction of excess staff. However, the said reform programs were not effectively implemented. The various studies undertaken by internal as well as international auditing experts have shown serious concern over the degrading financial situation leading them to the state of 'technically insolvent' banks. The KPMG Barents, an international auditing firm, that started its banking reform project in 1999 and presented its final draft report to NRB in 2000, revealed that RBB and NBL were deeply impaired in all areas of their operations.

The KPMG Barnet group pointed out poor bank governance, political interference and private sector self-dealings; lack of rational banking strategies as well as skills and international banking experience to support them; lack of independent, capable supervision; weak financial and management information; weak legal and accounting practices. There were deep and serious flaws in lending process, loan files and loan portfolio. The lack of business strategies, weak planning and budgeting practices had seriously deteriorated the banks' financial health. The low morale of employees, low pay scales, low skills and counter-productive union-oriented activities were other serious problems, the report showed. Moreover, the primitive management, information, record keeping and control system further aggravated the situation.

The report said that the estimated losses in these two banks was somewhere between Rs. 15-30 billion (US$ 220 to 435 million). These losses represent 4.5 to 8.5 percent of GDP and between 24 to 45 percent of Nepal's total budget in 1999. In 1998, the banks had losses of around US$ 450 million, which was equivalent to around 46% of the government's annual budget or 8.6 percent of GDP (Nepal Rastra Bank, 2004a).

The central bank, as per the recommendation of KPMG Barents, took the momentous move in March 2002 to dissolve the existing NBL board and finally handed over the management of NBL to the ICC Bank, Ireland, under management contract in mid-July 2002. Similarly, the central bank has selected a team of various domestic as well as international banking experts to carry out the management of RBB, the largest commercial bank in the country.

Defining the bank loans into four categories, the central bank has made the directives to the commercial banks to maintain sufficient provisioning for avoiding the possible crisis in the banking system when the borrowers fail to pay back their loans. As per the new NRB directives, the commercial banks have to maintain the following provisioning scheme for their outstanding loans:

1.	Standard:	Performing	1 %	
2.	Sub-standard:	Past Due 3 to 6 months	25%	NPLs
3.	Doubtful:	Past Due 6 to 12 months	50%	NPLs
4.	Loss:	Past Due above 12 months	100%	NPLs

The non-performing loan (NPL) problems have seriously deteriorated the financial health of two largest public banks. The amount of NPL is not only high but also increasing continuously as shown in the table 3.7. The share of NPL as percentage of total loans of these banks rapidly increased from 47 percent in 2001 to 60 percent in

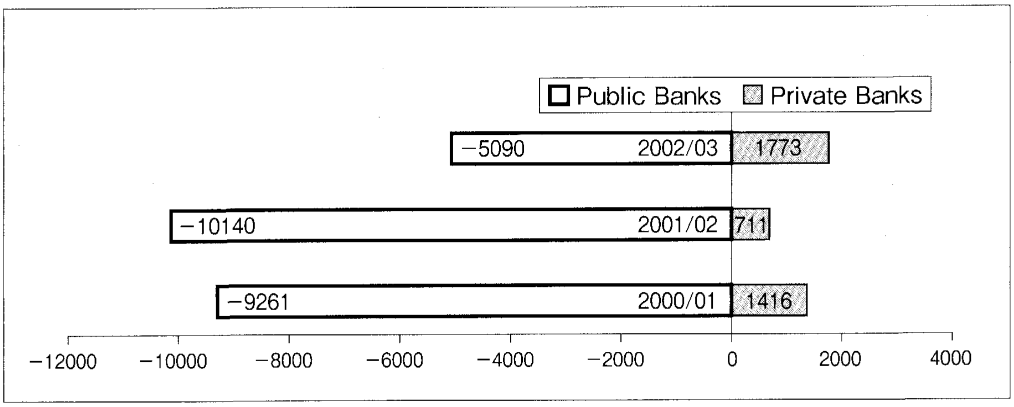
2003 whereas the corresponding figures for the private sector banks decreased from 11 percent in 2001 to 8 percent in 2003. This shows that the public sector banks have seriously undermined the overall health of Nepalese banking sector. The share of NPL as the percentage of total commercial bank loans stood at 29 percent in 2003. Despite the declining NPL and improving financial health of private sector banks, the national level banking indicators are poor due to the increasing NPLs and net losses in the public sector banks, which hold a significant market share. These banks are making huge losses every year in contrast to the improving financial position of private sector banks. However, it has been reported that these banks have made some progress in reducing NPLs and incurred profits for last two years. The assets and liabilities of NBL and RBB are given in the appendix (appendix III and IV).

Table 3.7. Non-performing Loans (NPL) of Commercial Banks (Rs. in million)

Banks	2001					2002		2003	
	Total Loan	NPL	NPL %	Total Loan	NPL	NPL%	Total Loan	NPL	NPL%
Nepal Bank Limited	20,491	10,373	51	19,253	10,834	56	18,132	10,965	60
Rastriya Banijya Bank	27,357	12,337	45	27,037	14,889	55	26,609	16,005	60
A. Public Banks (sub-total)	47,848	22,710	47	46,290	25,723	56	44,741	26,970	60
B. Private Banks (sub-total)	52,339	5,719	11	56,834	5,640	10	67,162	5,257	8
Grand Total (A+B)	100,187	28,429	28	103,124	31,363	30	111,903	32,227	29

Source- NRB, Various Publications

Figure 5. Commercial Bank Profitability, (Net Profits, Rs.in million)



Source- Annual Report (2003/04), Bank Supervision Department, NRB.

To sum up, the public sector banks (NBL & RBB) hold significant market share in the banking system. The combined assets, deposits, loans and investments of these two bank account for 49 percent, 36.3 percent, 38.2 percent, and 35 percent of the total banking system assets, deposits, loans and investments respectively (as of mid-July 2003). The credit-deposit ratio of NBL (53% as of 2004) is significantly lower than that of RBB (70%) implying the poor intermediary role. These banks have the largest number of branch network representing 55 percent of total commercial bank branches in 2004. These two banks have been playing the significant role in supplying the large amount of credits to corporate and other various sectors of the economy. They have significantly contributed to the economy by mobilizing the fragmented savings into the productive investments. Moreover, in addition to the normal commercial banking activities, these banks have been constantly supporting to carry out the government budgetary operations through their widespread branch network. In spite of the significant role they played in the economy, the financial as well managerial health of these banks was found seriously downgrading sine the early 1990s leading them into the state of technically insolvent banks. The various studies (CBPASS, KPMG) pointed out poor bank governance, political interference and private sector self-dealings; lack of rational banking strategies as well as skills and international banking experience to support them; lack of independent, capable supervision; weak financial and management information; weak legal and accounting practices. Consequently, these banks have been seriously engulfed by mounting non-performing loans and accumulated loss every year. Despite the continuous injection of capital, there has been no progress so far. In order to improve the situation of these banks, the immediate measures should be undertaken to ensure good corporate governance system and active monitoring mechanism so as to discourage the imprudent lending decision, insider-practices and excessive politicization.

IV. PERFORMANCE OF BANKING SYSTEM: COMPARATIVE ANALYSIS

This section compares the major performance indices of Nepalese banking system with that of South Asian developing and some selected industrial economies. The International Financial Statistics (IFS) and Fitch's Bankscope Databases are the major source of data for international comparison. The size, efficiency and competitiveness of the banking system have been analyzed here by using the various ratio measurements deflected by the size of the economy, i.e. by the GDP of respective countries. The size of financial intermediaries are measured by the liquid liabilities as percentage of GDP, the concentration indices are obtained by various techniques, such as M3 index, Gini-coefficient and Herfindahl Index. The banking sector activities in the private sector are measured by the ratio of bank credit to private sector to GDP. The efficiency of the banking system is measured by the ratios of net interest margin and overhead costs to GDP. These all ratio measures are adjusted with the average annual and end of the period CPI.

$$\{(0.5)*[F_t/Pe_t + F_{t-1}/Pe_{t-1}]\} / [GDP_t/Pa_t]$$

where, F is the variable under study (liquid liabilities, overhead costs, net interest margin, credit to private sector, etc); P_{at} and P_{et} are average annual and end period CPI respectively.

4.1. Liquid Liabilities

The liquid liabilities measured as a percentage of GDP reflects the size of financial intermediaries in relation to the size of economy. This ratio is generally used as an overall measure of financial sector development. The comparative statistics compiled from the IFS Database show the lower ratio in the developing countries than that of developed economies. Higher ratio indicates larger size of financial intermediaries. In other words, high liquid liabilities to GDP ratio imply higher financial deepening and vice versa. The statistics for Nepal and Bhutan are available only up to the year 2000. Instead of measuring the liquid liabilities, the broad money supply (M2) to GDP ratio can also be used for this purpose. However, this study uses IFS data that takes M3 as liquid liabilities. The ratio between M2 and M3 to GDP does not significantly differ in Nepal. Thus, liquid liabilities to GDP ratio is around 50 percent for Nepal in 2003 (if measured by using M2 instead of M3). The statistics clearly show the expansionary trend of financial intermediation as reflected by ratio that increased from 30 percent in 1990 to around 50 percent in 2003. India and Pakistan have higher ratio (60 % and 53% respectively in 2003) than other South Asian economies.

The high-income countries, on the other hand, have higher liquid liabilities to GDP ratio than low-income countries. However, the securities market-based economies, such as USA and UK, have substantially low ratio than bank-based economy, like Japan. The

Table 4.1. Liquid Liabilities as % of GDP (Developing Countries)

Year	Nepal	Bangladesh	India	Pakistan	Bhutan	Sri Lanka
1990	30	Na	40	38	21	32
1991	31	Na	41	37	23	33
1992	31	Na	42	39	25	35
1993	33	Na	42	43	25	36
1994	34	27	43	43	26	38
1995	36	Na	42	42	29	42
1996	36	Na	42	43	29	44
1997	38	29	44	45	32	42
1998	43	29	46	46	38	43
1999	44	29	48	45	39	45
2000	47	32	53	45	43	44
2001	Na	35	55	47	Na	46
2002	Na	37	59	51	Na	45
2003	Na	38	60	53	Na	46

Source- International Financial Statistics (compiled from World Bank Research Database)

Table 4.2. Liquid Liabilities as % of GDP (Developed Countries)

Year	Japan	USA	UK	Germany	Italy	Canada
1990	178	64	91	71	67	71
1991	177	64	90	65	68	75
1992	179	62	75	65	69	76
1993	183	60	61	70	68	76
1994	189	57	61	71	65	74
1995	193	56	66	70	61	75
1996	196	56	72	73	59	75
1997	187	56	82	75	55	75
1998	182	58	89	76	51	75
1999	191	59	95	Na	Na	72
2000	193	61	104	Na	Na	69
2001	197	65	109	Na	Na	73
2002	202	68	111	Na	Na	75
2003	169	67	113	Na	Na	75

Source- International Financial Statistics (Compiled from WB Research Database)

statistics reveal that the size of financial intermediaries is increasing in UK since last few years, despite the dominance of market based financial system in the country. The size of financial intermediation has been declining in Italy and remaining almost constant in Canada over the period 1990-2003 as shown in the following table.

4.2. Bank Concentration

The bank concentration, measured in terms of the ratio of the assets of largest 3 banks to the total commercial banking assets, measures the concentration of banking assets and competition among the sector (Demirguc-Kunt and Levine, 2001). In general, this ratio tends to be lower in the high-income countries where the level of competition is high. The public sector banks in Nepal hold significant share of total banking system assets, deposits, loans and investments. The comparative statistics show that the level of assets concentration is higher in Sri Lanka (68 %), Bangladesh (52%) and Pakistan (55%) than in Nepal (51%) while the ratio in India is 40 % in 2003 as shown in the following table.

Table 4.3. Bank Asset Concentration, % (Developing Countries)

Year	Nepal	India	Bangladesh	Pakistan	Sri Lanka
1996	80	34	64	78	99
1997	79	32	65	70	98
1998	72	32	63	69	82
1999	66	30	60	68	73
2000	64	28	57	72	73
2001	59	49	54	63	71
2002	55	41	53	59	68
2003	51	40	52	55	68

Source- Fitch's Bankscope Database (Compiled from WB Research Database)

As mentioned above, the level of concentration is relatively low in the developed economies. The concentration ratio is lowest in the USA (31 %) followed by Japan (33%) and Italy (41%) among the selected industrial countries in 2003. The ratio is highest in Germany (64%) followed by Canada (54%) in the same year. The table 4.4 compares the level of concentration among the seven industrial economies.

Table 4.4. Banking Assets Concentration, % (Developed Countries)

Year	Japan	USA	UK	Germany	France	Italy	Canada
1996	71	31	51	29	51	57	71
1997	75	30	47	77	55	47	58
1998	44	30	41	77	49	50	56
1999	43	33	40	67	52	49	53
2000	46	31	38	66	49	50	52
2001	43	31	38	64	50	50	54
2002	33	31	41	63	45	44	54
2003	33	31	43	64	47	41	54

Source- Fitch's Bankscope Database (Compiled from World Bank Research Database)

The above-mentioned concentration measure takes into account only three largest banks and uses assets of these banks as the major variable. There are various other techniques to measure the industry concentration. In order to evaluate market concentration and level of competition, we also employ the methods of Gini-coefficient and Herfindahl Index. The Gini- coefficient is used more often to gauge the income inequality. The same technique is used here to measure the degree of concentration of various banking variables such as assets, deposits, loans and advances, and investments. The following formula is used to calculate Gini-coefficient:

$$Gini = \frac{2}{\mu n^2}\sum_{i=1}^{n} iX_i - \frac{n+1}{n}$$

where, μ is the mean of variables under study (assets, capital, deposits, loans and investments), n is number of observations in ascending order and Xi is cumulative share of variables in descending order. The value of G ranges between 0 and 1. The value close to zero implies less concentration and vice versa.

The Herfindahl Index is a well-known measure of industry concentration. This index ranges from a low of zero, indicating perfect competition, to the highest of 10,000, indicating complete monopoly. Greater values mean greater concentration, less competition, and more market control held by individual firms. The index is defined as the sum of the squared shares of market participants, which is given mathematically as:

$$H = \sum_{i=1}^{n} \alpha_i^2$$

where, H is Herfindahl Index, α i is the share of variables mentioned above. This index is taken to be better concentration index than Gini-coefficient as the Herfindahl index does not take into account the number of companies and focuses on the size only. The calculated index is then compared with the level of concentration as given in the following Herfindahl concentration table.

Table 4.5. Concentration Level

Level	**Concentration Ratio**	**Herfindahl Index**
High	80 to 100%	1,800 to 10,000
Medium	50 to 80%	1,000 to 1,800
Low	0 to 50 %	0 to 1,000

The empirical results are presented in the following table and figure. It is clear from the table that the commercial bank assets are highly concentrated whereas the level of concentration of the paid-up capital is relatively lower than other variables. The level of concentration has significantly declined over the period 1996-2003 implying that the market is gradually tending to be more competitive and the dominance of few (particularly, two public sector banks) and large financial institutions is gradually declining.

Table 4.6. Herfindahl Concentration Index

Particulars	1996	1997	1998	1999	2000	2001	2002	2003
Assets	2856.24	2469.23	2361.41	2127.41	1952.25	1747.31	1776.66	1643.97
Deposits	2291.00	2091.32	2032.54	1936.24	1704.56	1438.76	1374.42	1244.68
Paid-up capital	2447.26	2192.19	2051.06	1496.15	1391.71	1061.65	817.33	693.92
Loans and Advances	2584.12	2429.02	2269.10	2159.10	1859.67	1504.60	1408.89	1202.43
Investment	1903.78	1785.73	2469.28	2174.20	2064.88	1779.77	1656.11	1507.81

Figure 6. Herfindahl Concentration Index

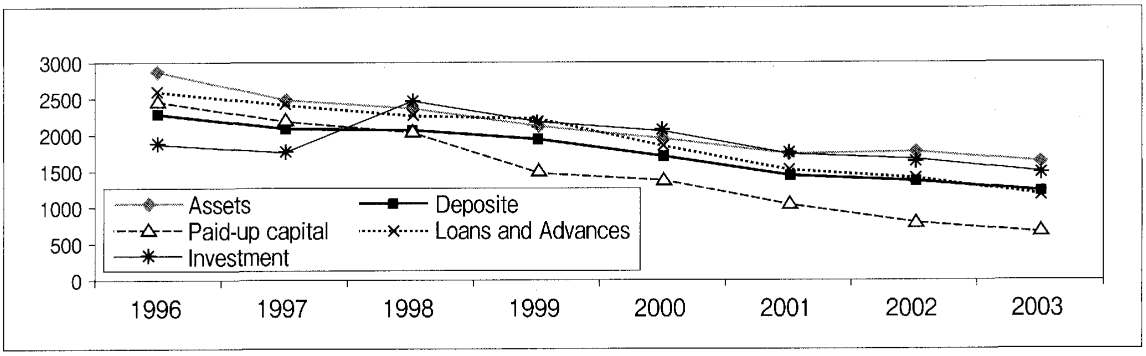


Table 4.7. Gini Concentration Index (1996-2003)

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Bank Assets	0.60	0.65	0.63	0.62	0.59	0.61	0.57	0.59	0.61	0.60
Deposits	0.58	0.52	0.57	0.57	0.54	0.58	0.53	0.53	0.55	0.53
Paid-up Capital	0.58	0.59	0.53	0.51	0.47	0.44	0.42	0.33	0.25	0.17
Loans and advances	0.59	0.62	0.60	0.59	0.56	0.60	0.54	0.53	0.53	0.49
Investments	0.62	0.66	0.52	0.53	0.61	0.64	0.65	0.63	0.63	0.59

The concentration indices obtained from the Gini-coefficient also give the similar results and are consistent with the fact that Nepalese banking system is highly concentrated (in terms of assets, loans, deposits, etc.) to few numbers of banks. A trend analysis depicts that the level of concentration has substantially declined over the period and will ultimately come down in the future.

4.3. Overhead Costs

The overhead costs measured in terms of the ratio of bank overhead costs to the total assets of the banks simply reflect the efficiency measure of the banking system. The excessive overhead expenditures may reflect waste of resources. However, this ratio needs a very careful interpretation. It should be noted that the competitive banks may undertake substantial investments to provide high-quality financial services to the costumers. These productivity-enhancing investments may increase the overhead costs. In this sense, the low overhead costs may reflect insufficient competition and inadequate investment in providing quality services. Thus, overhead costs do not reflect the banking system efficiency unambiguously. Despite these limitations, the ratio is widely used for measuring the efficiency of the banking system. Lower the ratio, the more efficient the system is considered to be. This study compiles the data from the International Financial Statistics and compares the overhead costs among the selected developing as well as developed countries. The statistics show very similar efficiency measure among the South Asian Countries as shown in the table 4.8.

Table 4.8. Overhead Costs, % (Developing Countries)

Year	Nepal	India	Bangladesh	Pakistan	Sri Lanka
1996	3	3	2	3	3
1997	2	2	2	3	3
1998	2	2	2	3	3
1999	2	2	2	3	3
2000	2	2	2	3	3
2001	2	2	2	3	3
2002	2	2	2	2	3
2003	2	2	2	2	3

Source- Fitch's Bankscope Database (Compiled from World Bank Research Database)

An ambiguous fact to be noted here is that the overhead costs among the developed countries are slightly higher than that of developing economies. This does not necessarily mean that the banking system in the former countries is more inefficient than later. This may reflect the fact that the banks in those countries have undertaken higher investments to provide high-quality financial services and products. The overhead costs of Japanese banks are slightly lower among the seven industrial economies. The comparison of the overhead costs among the seven industrial economies is given in the table 4.9.

Table 4.9. Overhead Costs, % (Developed Countries)

Year	Japan	USA	UK	Germany	France	Italy	Canada
1996	2	4	4	3	4	3	5
1997	1	4	3	3	4	4	4
1998	2	4	3	3	4	4	4
1999	2	4	3	3	4	4	4
2000	2	4	3	4	4	5	4
2001	3	4	3	4	4	5	5
2002	3	4	4	4	4	5	4
2003	2	4	4	4	4	5	3

Source- Fitch's Bankscope Database (Compiled from World Bank Research Database)

4.4. The Net Interest Margin

The net interest margin, measured by the banks' interest income minus interest expenses as percentage of total assets, is used to measure the efficiency and competition in the banking system. Remaining the other things same, tighter interest margin is considered as the greater competition and efficiency. However, there are basically two limitations of this measure. First, net interest margin does not take into account fees and commission incomes that can change the effective interest rate. Second, this indicator may not be a good measure if the government or central bank capitalizes the bank by purchasing bond below the market rate. Despite these limitations, this is one of the most widely used measures of the costs of financial intermediations. This ratio declined from 5 percent in 1996 to 3 percent in 2003 in Nepalese banks implying improved intermediation costs as a result of increasing level of competition in the banking sector.

On the other hand, the high-income countries also have the similar ratio of net interest margin to total assets implying no significant differences in the level of efficiency in the banking system among these countries. The data show that Japan has relatively small ratio than that of other industrial economies implying greater efficiency in the banking system. The following table compares net interest margin among seven industrial economies.

Table 4.10. Net Interest Margin, % (Developing Countries)

Year	Nepal	India	Bangladesh	Pakistan	Sri Lanka
1996	5	3	2	4	5
1997	5	3	2	3	5
1998	4	3	2	4	4
1999	3	3	2	3	4
2000	3	3	2	3	4
2001	3	3	3	4	3
2002	3	3	2	3	3
2003	3	3	2	3	4

Source- Fitch's Bankscope Database

Table 4.11. Net Interest Margin, % (Developed Countries)

Year	Japan	USA	UK	Germany	France	Italy	Canada
1996	1	4	3	3	3	4	3
1997	1	5	3	3	3	4	2
1998	2	4	4	3	3	4	3
1999	2	4	3	3	3	3	2
2000	2	4	4	3	3	3	2
2001	2	4	3	3	3	3	4
2002	2	4	3	3	3	3	3
2003	2	4	3	3	3	3	3

Source- Fitch's Bankscope Database (Compiled from World Bank Research Database)

4.5. The Claims on Private Sector

The claims on private sector given by the ratio of deposit money bank credits (and other claims on) to the private sector as the percentage of GDP measures the banks' activities in the private sector. The IFS data for Nepal and Bhutan are not available since 2001. However, the data obtained from the domestic sources (Nepal Rastra Bank & Ministry of Finance) provide the similar measure showing that the banks' activities in the private sector are increasing over the period 1990-2003. The claims on private sector to GDP in Nepal increased from 12 percent in 1990 to 28 percent in 2000. This ratio increased to 34 percent in 2003. The comparative statistics reveal the fact that the banks' activities in the private sector are increasing relatively faster in Nepal than in other South Asian economies as shown in the table below. The table also shows the ratio is significantly lower in the developing countries than that of developed economies.

The ratio of banks' claims on private sector to GDP is considerably higher in Japan, UK and Germany than in other G7 economies implying the large presence of banking

Table 4.12. Claims on Private Sector by Deposit Money Banks as % of GDP

Year	Nepal	Bangladesh	Bhutan	Pakistan	India	Sri Lanka
1990	12	Na	4	24	24	18
1991	12	Na	5	22	23	13
1992	12	Na	6	22	23	8
1993	13	Na	7	24	23	9
1994	15	15	7	23	22	10
1995	20	Na	7	23	22	20
1996	22	Na	6	24	22	29
1997	22	22	8	24	22	27
1998	25	22	9	24	23	27
1999	27	22	8	25	24	28
2000	28	23	8	26	27	27
2001	Na	24	Na	26	28	28
2002	Na	26	Na	26	30	27
2003	Na	27	Na	27	31	28

Source-International Financial Statistics (Compiled from World Bank Research Database)

activities in the private sector. The comparative IFS data show the smallest ratio in the US because of the dominance of securities market in the financial system. However, this ratio is declining in Japan as the sources of finance are gradually shifting from banks to securities market in the recent years. Despite the dominant role of securities market in UK, the ratio of the banks' claim on private sector to GDP is continuously increasing over the period. This shows that banking system is increasing its activities in the private sector, though the securities markets are the major sources of corporate finance.

To sum up, the international comparison based on IFS and Fitch's Bankscope Database shows that Nepalese banking system measured in terms of size, level of competition, and efficiency does not significantly differ from that of South Asian developing economies. Nepal's liquid liabilities to GDP ratio, the measure of the size of financial intermediaries in relation to the size of economy, is comparable to that of Pakistan and Sri Lanka, higher than that of Bhutan and Bangladesh but lower than India. This ratio in the developed countries is significantly higher showing the larger size of financial intermediaries. The bank assets concentration indices show highly concentrated banking assets in Sri Lanka than in Nepal, Pakistan and Bangladesh. The banking asset in India is less concentrated than in other South Asian countries. Moreover, the declining values of concentration indices for bank assets, deposits, loans and investments measured by Gini-coefficient and Herfindahl Index show that the level

Table 4.13. Claims on Private Sector by Deposit Money Banks as % of GDP

Year	Japan	USA	UK	Germany	Italy	Canada	France
1990	114	61	112	93	53	47	91
1991	115	58	112	87	56	51	95
1992	117	53	111	90	59	52	96
1993	116	51	108	96	61	54	95
1994	114	50	107	99	59	56	89
1995	114	52	110	101	57	57	86
1996	112	53	114	105	55	60	85
1997	111	53	116	110	55	65	82
1998	115	55	116	114	57	67	Na
1999	117	57	117	117	64	64	Na
2000	114	60	124	117	72	63	82
2001	113	63	132	119	77	67	86
2002	110	63	136	119	79	68	87
2003	105	63	141	117	83	68	88

Source-International Financial Statistics

of competition is gradually increasing. The bank assets concentration in the developed countries is rather smaller, however, in Germany, it's very high. The overhead costs as percentage of GDP gives ambiguous result. The lower ratio generally means the higher banking system efficiency. But, competitive and efficient banks may have higher investments to provide high-quality services and hence have higher overhead costs. It is due to this reason that the overhead costs in the developed banking system are not notably lower (or may be higher) than that of underdeveloped banking system. Similarly, the differences in the net interest margin, another measure of efficiency and competition, among the countries under study is not notably significant. Finally, the ratio of bank's private credit to GDP, a measure of banking activities in the private sector, is much lower in the developing countries than in developed ones. This implies relatively small involvement of banking activities in the private sector.

V. CONCLUSION

Nepal has a bank-based financial system. Compared with securities market, the banking sector has relatively longer historical foundation, established institutional settings and better growth and development trend. The securities market has very small share of corporate finance compared with bank credits. Nevertheless, the overall

Nepalese financial system is still an underdeveloped bank based model while comparing with other developed as well as developing economies. The banking sector is composed of 17 commercial banks, 34 development banks, 59 finance companies and many micro-credit banks and NGOs licensed to conduct banking activities. The decade of 1990s remained as a 'good time' for Nepalese banking industry in terms of growth and product innovation. However, the situation turned sour as the economy gradually began to shrink since 2002. The securities market is very small and passing through its infancy. The banking system, on the other hand, is highly concentrated with two largest and problem-led public sector banks. Although the market share of these banks has been declining since the early 1990s, the financial system is still highly dominated by them. During the 1990s, many efficient and well-managed private sector banks with diversified services and products of international standard entered into the market.

The financial deregulation created private-sector-friendly environment that resulted into the significant growth of banks and finance companies during the 1990s. The reforms in the financial system, particularly in the banking sector, were brought into two phases. The first phase consisted of the curative measures, which were brought about by making the banking sector more market-oriented and impart competition among them. The second phase consisted of the preventive measures that aimed to ensure long-run growth and development of banking system.

The commercial banking sector comprises the core of Nepalese financial system. This sector alone represents 80 percent of total assets, 72 percent of total loans and advances, 88 percent of total investments and 81 percent of total deposits of the overall banking system (as of 2003). There is highly asymmetric distribution of assets, deposits, loans and investments within the industry. However, the situation is gradually improving in the recent years, as there has been rapid expansion of financial institutions in the private sector.

The banking and overall financial system is highly dominated by the problem-led public sector banks (NBL and RBB) characterized by operational inefficiencies, poor governance, weak management, insider-control practices, imprudent lending decision and politicization as shown by various studies (including CBPASS, KPMG, etc). These two banks account for 49 percent of total assets, 36.3 percent of the total deposits, 38.2 percent of total loans and 35 percent of total investments of overall banking system (as of mid-July 2003). These banks have been playing significant role in credit supply, deposit mobilization, government budgetary operations and central banking activities, especially in the remote areas of the country. Despite their notable contribution to the economy, these two banks have been financially paralyzed and technically insolvent due mainly to the three mistakes, namely, imprudent lending decision, insider-practices and excessive politicization, made especially in the past. The increasing volume of non-performing loans and accumulated loss in these banks have seriously undermined the health of overall banking system.

The international comparison based on IFS and Fitch's Bankscope Database shows that Nepalese banking system measured in terms of size, level of competition, and efficiency does not significantly differ from that of South Asian developing economies. The size of the financial intermediaries, measured by the ratio of liquid liabilities to GDP, is relatively smaller in the developing countries than in developed ones. Similarly, the comparative statistics show that the level of assets concentration is higher in the banking system of developing economies. The declining concentration indices obtained from Gini-coefficient and Herfindahl index show that the level of competition is gradually improving in Nepal.

The net interest margin and overhead costs are not significantly different among the South Asian countries; the differences are even not remarkable between the developing and developed countries under study. This may be due to the fact that the competitive and efficient banks may have higher investments to provide high-quality services and hence have higher overhead costs. The data reveal that the ratio of bank claims on private sector to GDP for the developed countries is significantly higher than that in developing countries. However, the ratio in the developing countries has been increasing as the financial markets in these countries underwent significant deregulation thereby leading to increased private sector participation in the financial system.

Finally, the banking sector is the major source of external finance and the single largest component of Nepalese financial system. It is not only the major supplier of external funds, but also the provider of all sorts of available financial services to the people throughout the country. In spite of its rapid expansion during the nineties, there exist a number of challenges in improving the corporate governance and monitoring system of the public sector banks. The increasing NPLs and huge amount of accumulated losses in these banks have not only spoiled the depositor's money and banks' credibility, but also seriously undermined the overall health of financial system and economy as a whole. Several attempts have been made to improve the financial condition of these banks but the outcomes are always far from the expected ones. The state owned enterprise (SOE) sector is one of the major corporate clients of these banks. Unless the financial condition of the former is improved, there is less possibility of repayment of the past due loans and improve the NPL problems originating from state owned enterprises. So, the most appropriate measure is to simultaneously privatize both the banking and non-bank SOEs. The process should be initiated from the reduction of government's direct role in the operation and management of these enterprises. The gradual transformation of the control rights from the sate to private sector is the most appropriate policy measure to improve the financial as well as managerial condition of public sector banks. For the private banks, the ownership concentration should be diversified so as to improve the transparent and accountable corporate governance and monitoring mechanism.

Policy Implication

There have been various efforts and programs launched in support of donor agencies to reform Nepal's financial sector since the early 1990s. As the result of introduction of open and liberal financial policies, the private banking sector witnessed tremendous growth both in terms of both qualitative as well as quantitative aspects. However, the reforms in the public sector banks have not been so effective. The evidences are clear as shown by the increasing NPLs and accumulated losses. Moreover, there have been no improvements in corporate governance and monitoring system in these banks. In spite of the repeatedly spelled out policy agenda, the government is still reluctant to privatize these banks. The privatization of these banks is the only solution to discourage the rent seeking behavior and improve the financial, managerial as well as corporate governance system. Due to the increasing number of financial institutions in the private sector, the share of these banks in the total banking system assets, deposits, loans and investments are gradually declining. However, it is still high by any standard.

Of course, there are many practical difficulties to immediately privatize these banks as no private entities or persons are eagerly interested to buy the share of these financially sick industries. The process can be made easy by gradually solving the problems of NPLs and effectively implementing strict credit monitoring mechanism in the first place. The willful defaulters should be brought under strict legal action, which helps banks to recover their bad loans and improve the financial position. The government representation in the management board has led to the inefficient operation, poor corporate governance and insider lending practices in these banks. So, the first step to initiate the proper reform is to make these banks at least suitable for privatization by two ways: first, solving the NPL problems by strict action against willful defaulters, the major cause of mounting NPL in Nepalese banking system, and discouraging insider practices and imprudent lending decisions; second, improving the corporate governance and monitoring system by giving up government intervention in the management and operation of these banks. These actions should be made in the process of privatization. When the financial conditions become normal or relatively better, the private investors become interested to invest in the share of these banks and the problems can be solved as the privatization enhances the competitiveness and efficiency in the market.

The concentrated ownership structure is one of the reasons for weak disclosure and transparency in the Nepalese financial system. Although the private banks are relatively in the better position than public sector banks, a small number of majority shareholders (promoters) in the former always dominate large number of minority shareholders in the process of corporate decision-making. Such practices may lead to insider lending and non-transparent governance system. The diversified ownership structure discourages such practices and at the same time enhances the scope of securities market.

Finally, the Nepalese banking system is concentrated in the urban areas. Due to the degrading security situation and downsizing economic activities, the existing branches in the remote areas are being closed down. A stable politico-economic condition is immensely essential to mobilize the huge amount of fragmented savings through banking channel and provide formal credits and other banking services to the largest fraction of population living in countryside.

APPENDIXES

Appendix I

Major Financial Institutions (1956-1977)

S.N.	Institutions	Established in	Remarks
1	Nepal Bank Limited	1937	First commercial bank
2	Nepal Rastra Bank	1956	Central bank
3	Industrial Development Bank	1957	Converted into NIDC, 1959
4	Nepal Industrial development Corporation (NIDC)	1959	
5	Employee's Provident Fund Corporation	1962	
6	Co-operative Bank	1963	Merged with ADB/N, 1968
7	Rastriya Banijya Bank	1966	Second commercial bank
8	Land Reform Savings Corporations	1966	Merged with ADB/N, 1973
9	National Insurance Corporation Ltd.	1967	First insurance company
10	Agricultural Development Bank (ADB/N)	1968	
11	Nepal Insurance Corporation	1968	Insurance company
12	Credit Guarantee Corporation	1744	
13	Securities Marketing Center	1977	Converted into Securities Exchange Center in 1984
14	Postal Saving Offices	1977	

Source: Nepal Rastra Bank (1996)

Appendix II

Sources and Uses of Funds of Commercial Banks

Particulars	1996	1998	2000	2002	2004*
Capital Fund	3560.7	4955.7	6729.3	10202.5	12229.3
Paid-up Capital %	63.8	59.8	60.4	63.0	65.0
Statutory Reserves %	24.9	25.7	29.4	24.9	24.6
Other Reserves %	11.4	14.5	10.2	9.5	9.8
Retained Earnings %				2.6	0.5
Deposits	71400.5	102598.2	154943	185144.7	215136.6
Current %	18.6	15.9	13.1	13.1	12.7
Savings %	36.3	36.0	42.4	45.3	49.2
Fixed %	41.2	44.4	40.1	34.7	30.1
Call %	1.0	1.7	2.4	5.7	6.8
Others %	3.1	2.0	1.9	1.2	1.3
Borrowings	885.3	887.0	3346.6	2349.5	4324.2
From Central Bank %	26.0	43.0	12.8	49.7	22.5
Inter Bank %	74.0	57.0	87.2	40.6	29.8
Foreign Bank %	0.0	0.0	0.0	9.7	47.7
Financial Institutions %		0.0	0.0	0.0	0.0
Others	24874.9	36987.1	44452.6	77221.2	87343.7

Sources of Funds	100721.4	145428.0	209471.5	274918	319033.8
Liquid Funds	18206	33184.1	48240	49937.2	30762.8
Cash in hand %	13.4	8.7	7.3	9.8	12.1
FC in hand %	3.3	2.3	1.3	1.2	1.8
Balance with NRB %	35.7	42.5	35.1	46.4	40.1
Bal. with Domestic Banks %	-0.9	1.2	1.4	1.9	2.6
Bal. held abroad %	42.9	27.7	30.3	14.1	6.7
Call Money %	5.7	17.6	24.6	26.7	36.7
Investments	8585.3	10857.5	17967.3	34209.8	53682.4
Government Securities %	90.6	97.6	98.0	83.5	86.2
Share, Deben & other Inv. %	1.5	2.4	2.0	16.5	13.8
NRB Bond %	7.9				
Loans and Advances	50891.1	68618	96324.9	113174.6	133437.4
Government Enterprises %	2.9	1.8	2.2	2.3	2.1
Private Sector %	93.1	94.7	95.8	96.3	97.1
For. Bills P. & D. %	3.6	3.3	1.9	1.2	0.7
Foreign A.B.C. %	0.4	0.2	0.2	0.1	0.0
Interest Accrued	7723.2	10618.6	16125.8	23742.8	32805.3
Government Enterprises %	11.2	2.1	2.3	1.3	0.8
Private Sector %	88.8	97.9	97.7	98.7	99.2
Others	15315.8	22149.8	30813.5	53853.6	68345.9
Uses of Funds	100721.4	145428	209471.5	274918	319033.8

As of mid-January, Source- Compiled from Banking and Financial Statistics, mid-July 2004, NRB

Appendix III

Assets and Liabilities of Nepal Bank Limited (Rs. in million)

Year (Mid-July)	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004*
1. Capital Fund	586	625	703	853	882	1,015	1,044	1,126	1,350	1,449	1,064
2. Deposits	17,856	18,749	19,855	21,543	28,145	33,093	35,579	35,529	34,060	34,737	35,775
Current %	18	18	19	16	16	13	14	14	13	13	14
Saving %	34	41	43	43	39	43	50	57	58	62	62
Fixed %	46	39	35	39	44	43	35	28	29	24	24
Call deposits %	-	-	-	-	-	-	-	-	0	0	-
Others %	2	2	2	2	1	1	1	1	0	0	0
3. Borrowings	3	178	33	27	244	284	236	266	215	52	50
4. Others	6,660	4,702	5,027	6,756	8,664	9,955	9,262	13,947	28,192	30,091	26,547
5. Total Liabilities (1+2+3+4)	25,104	24,253	25,618	29,178	37,934	44,348	46,120	50,868	63,817	66,330	63,436
6. Liquid Funds	3,806	4,362	4,001	5,168	7,167	8,035	7,649	8,051	8,064	4,771	3,525
7. Investments	6,814	4,238	1,999	683	4,475	5,119	5,462	6,776	7,153	11,783	13,146

Government securities %	65	87	93	75	99	99	99	99	99	99	96
Share, Deben. & Others %	1	1	3	25	1	1	1	1	1	1	4
NRB Bond %	34	12	5	-	-	-	-	-	-	-	-
8. Loans and Advances	9,049	11,849	14,856	18,069	19,472	22,395	22,864	22,062	20,998	19,266	18,793
Government Enterprises %	3	3	4	5	3	3	4	3	3	4	4
Private Sector %	92	94	93	92	95	95	95	96	96	95	96
Others %	5	3	3	3	3	2	1	2	1	1	1
9. Interest Accrued	1,648	1,812	2,211	2,677	3,324	4,288	5,327	6,958	8,793	9,773	10,901
10. Other Assets	3,789	1,993	2,550	2,582	3,497	4,511	4,818	7,020	18,810	20,737	17,072
11. Total Assets (6+7+8+9+10)	25,104	24,253	25,618	29,178	37,934	44,348	46,120	50,868	63,817	66,330	63,436

Source- Compiled from various issues of Banking and Financial Statistics, NRB, * As of mid-January

Appendix IV

Summary of Assets and Liabilities of Rastriya Banijya Bank, Rs. in million

Fiscal Year (mid-July)	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004*
1. Capital Fund	1,132	1,334	1,334	1,385	1,391	1,441	1,483	1,507	1,538	1,558	1,464
2. Deposits	16,283	18,780	20,725	22,016	26,968	33,329	38,411	40,500	38,965	39,309	39,886
Current %	15	17	18	15	14	11	11	12	12	12	12
Saving %	29	32	33	35	35	37	41	46	49	53	57
Fixed %	53	49	44	47	49	50	46	41	39	35	31
Call %	-	-	-	1	0	0	0	0	0	0	0
Others %	3	3	5	2	2	1	1	1	0	0	0
3. Borrowings	39	248	203	214	265	272	152	147	156	162	86
4. Others	10,157	11,628	16,580	18,840	21,577	18,746	25,004	31,491	35,459	41,070	43,240
5. Total Liabilities (1+2+3+4)	27,611	31,990	38,842	42,455	50,201	53,788	65,049	73,645	76,118	82,098	84,676
6. Liquid Funds	5,355	5,910	6,015	6,639	10,318	10,278	13,633	14,560	15,090	8,159	4,606
7. Investments	3,614	2,798	1,990	1,443	2,372	2,785	4,337	5,657	4,171	4,233	5,887
Government securities %	74	96	99	97	98	97	98	99	98	98	97
Share, Deben & Others %	0	1	1	3	2	3	2	1	2	2	3
NRB Bond %	26	3	-	-	-	-	-	-	-	-	-

8. Loans and Advances	10,732	13,999	18,405	18,922	22,405	26,340	29,141	28,425	28,516	28,259	27,729
Government Enterprises %	4	2	3	1	1	1	0	2	2	2	1
Private Sectors %	91	94	93	96	96	97	98	97	97	97	99
Others %	4	3	4	4	3	2	2	1	1	1	0
9. Interest Accrued	3,406	4,064	5,161	5,863	6,546	7,638	9,268	11,277	13,302	15,401	18,275
10. Other Assets	4,504	5,219	7,271	9,588	8,560	6,747	8,670	13,726	15,040	26,046	28,179
Total Assets (6+7+8+9+10)	27,611	31,990	38,842	42,455	50,201	53,788	65,049	73,645	76,118	82,098	84,676

Source- Compiled from various issues of Banking and Financial Statistics, NRB.

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