Internship Report on

The Effects of Default Loan on Bank Profitability in Bangladesh

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Letter of Transmittal

15th January 2022
Md.Shahbub Alam
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Subject: **Submission of Internship Report.**

Dear Sir,
With humble honor and respect, I am submitting my internship report on "**The Effects of Default Loan on Bank Profitability in Bangladesh**". As per partial accomplishment of the requirements for the BBA degree, this internship has been carried out under the supervision of you.

This report is an integral part of our academic courses in completion of the BBA program which has given me the opportunity to have an insight into the core part of topic. I hope this report reflects on the contemporary issues on the finance area that are being practiced by organizations in our country.

In completing the report, I tried my best to blend all my knowledge and imparted every available detail and also attempted to avoid unnecessary amplification of the report.

I humbly request you to accept this report for your kind evaluation.

Sincerely,

MD. MAHEDI HASAN
ID: BBA-1903018084
Department of Business Administration
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Student's Declaration

I, the undersigned, a student of Business Administration, Department of BBA program, major in
Finance of Sonargaon University (SU) do hereby declare that the internship report on "**The Effects of Default Loan on Bank Profitability in Bangladesh**" is the original one and has been prepared by myself and has not been submitted anywhere for any degree,diploma,title or recognition.

The report was prepared under the supervision of **Md. Shahbub Alam, Lecturer,** and Department of Business Administration of Sonargaon University (SU).

Sincerely,

MD. MAHEDI HASAN
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Letter of Authorization

Certified that this project report titled **“The Effects of Default Loan on Bank Profitability in Bangladesh”** is the bona fide work of **Md.Mahedi Hasan**, who carried out the study under my supervision. Certified further that to the best of my knowledge the work reported herein does not form part of any other project report or dissertation on the basis of which degree or award was conferred on an earlier occasion on this or any other candidate.

Md. Shahbub Alam
Lecturer
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Acknowledgement

At first I want to express my deep gratitude to the Almighty, the most merciful for his kindness to give me the ability to complete this report successfully. I extend my deep gratitude to my supervisor Md.Shahbub Alam, Lecturer, Department of Business Administration of Sonargaon University (SU) for his guidance, suggestions, and encouragement for the preparation of this report. Without his guidance I could not have finished this work on time.

He provided me full support and ideas necessary in analyzing the industry and thus to accomplish my goal. To conclude, I am also grateful to all of the respected teachers of the Bachelor of Business Administration for their continuous inspiration, assistance throughout these years.

Executive summaries

Bangladesh has done well in the economic development index. The picture of GDP's (Gross Domestic Product) growth rate is very impressive. Bangladesh has been able to keep GDP growth intact at six and a half. Recently, we got the status of developing country. With the goal of getting SDG in 2030, we have the goal of going to the developed country by 2041.

There is some mixed reaction in our financial sector, especially in the Banking sector. Clearly, the size of our default loan is increasing day by day. According to the central bank information, the government commercial banks are more likely to have huge default loans. Also private commercial Banks are plagued by this problem.

In order to become a developed country, the banking sector needs special reforms to control the default (Non-performing) loan.

List of Abbreviations

BB	Bangladesh Bank
NPLs	Non-performing Loans
ROA	Return on Assets
SBs	Specialized Banks
SCBs	State -owned Commercial Banks
FCBs	Foreign Commercial Banks
PCBs	Private Commercial Banks
DL	Default Loan

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Chapter: 01
Introduction

1.1 BACKGROUND OF THE STUDY

In the last few years, the bank sector of Bangladesh is passing through a difficult time. Experts are claimed that increasing trend of Non-performing loan one of the big factor for this crisis. There is no way but to reduce the defaulted loan in case of stability in the banking. The lack of proper supervision and absence of good governance has resulted in the dreadful culture of default loans in the banking of Bangladesh. According to the BB report "The volume of Non-performing loans Ratio stood at 8.1 % in Dec 2020, compared with the ratio of 8.9 % in the previous quarter despite close monitoring of the central bank. The NPLs rose to Tk. 961.02 billion as financial year of 2020, from Tk. 943.03 billion on the previous year (2019), according to Bangladesh Bank's (BB) latest statistics. It was Tk. 594.0 billion as in 2015.

Nevertheless, some adverse contributory factors are still yet to vanish from banking operations and have been impacting the whole credit operations of the commercial banking sector of Bangladesh adversely. Due to satisfactory level of good governance practices, Bangladesh's economy has been performing a very promising role over the last few years in comparison with other neighboring countries in South Asian region. In the fiscal year of 2011 GDP growth rate of Bangladesh was 6.7% which is third highest growth rate among neighboring countries- Sri Lanka with 8.3%; India 6.9%; Nepal 3.9%; Pakistan 2.4%. Evidently, the constant improvement of the service sector's health in Bangladesh has not only compensated the fading agricultural sector but also, has initiated a true dynamic pace to the country's national economy. In the financial year of 2010-2011, the service sector of Bangladesh alone contributed more than 23% of GDP (Bangladesh Bank, 2011). Financial Intermediaries (Bank, Insurance company, Mortgage etc), are the key participant has gained a significant growth of 9.39% and contributed a very important portion of 0.94% in GDP of 2011. It is to be mentioned here that, the present growth in the financial intermediation is the reflection of positive and healthy movement of the commercial banking sector of Bangladesh. Ahmad and Khanal (2007) argued that this promising economic movement is the outcome of successful operations of PCBs of Bangladesh even though, the major share of which are controlled by SCBs. Private commercial banks in Bangladesh have been appeared as the most potential business sector over last few decades. Privately held commercial banks have recently outperformed the nationalized banking sector in different sides. According to the Bangladesh Bank (2011) the privately owned banks holding about 61.4% of total deposit (i.e. BDT 2505.9 billion of total deposit of BDT 4082.7 billion), comparing nationalized bank's 27.5% (i.e. BDT 1123.6 billion of total deposit of BDT 4082.7 billion) and PCB's 59% of total assets (that is, BDT 3205.4 billion of total assets BDT 5431.5 billion) as compared to SCB's 28.8% of total assets (i.e. BDT 1564.9 billion of total asset BDT 5431.5 billion).

The number of privately owned commercial bank stood at 30 with 2912 branches all over the country in comparison with 4 nationalized commercial banks with 4148 branches (Bangladesh Bank, 2011).It can also be observed in different reports that, the privately held commercial banks have been maintaining a healthy loan recovery rate, which is well above the rate maintained by the public commercial bank. Bangladesh Bank, Quarterly (2010) showing the loan recovery rate of privately owned banks has increased considerably by 42.7% while the recovery rate of public commercial banks has increased only 15.6% over the last few years. Private commercial banks recovered BDT 56 billion, where publicly owned banks could able to recover BDT 17.5 billion outstanding. Loan recovery comparison of the two banking sectors portrays the disappointing scenarios of SCBs and also shows PCBs with nonperforming loans i.e. 3.5% as compared to SCBs' 14.1% (Bangladesh Bank, 2011). Nevertheless, the contributions of SCBs are not negligible, rather, because of its several roles like: large geographical coverage, effective mobilization of fund throughout the country, huge employability, good motivation for small and large deposit, immense rural eco-social development program, provides an extra height to this banking sector.

THE REAL PICTURE OF DEFAULT LOAN: In the Figure-1 below, an overall picture of the defaulted loan will be available in the banking system. In 2011, the amount of this loan was 226.5 billion in taka which is 961.2 billion in 2020. The amount of these loans has increased significantly in the last ten years.

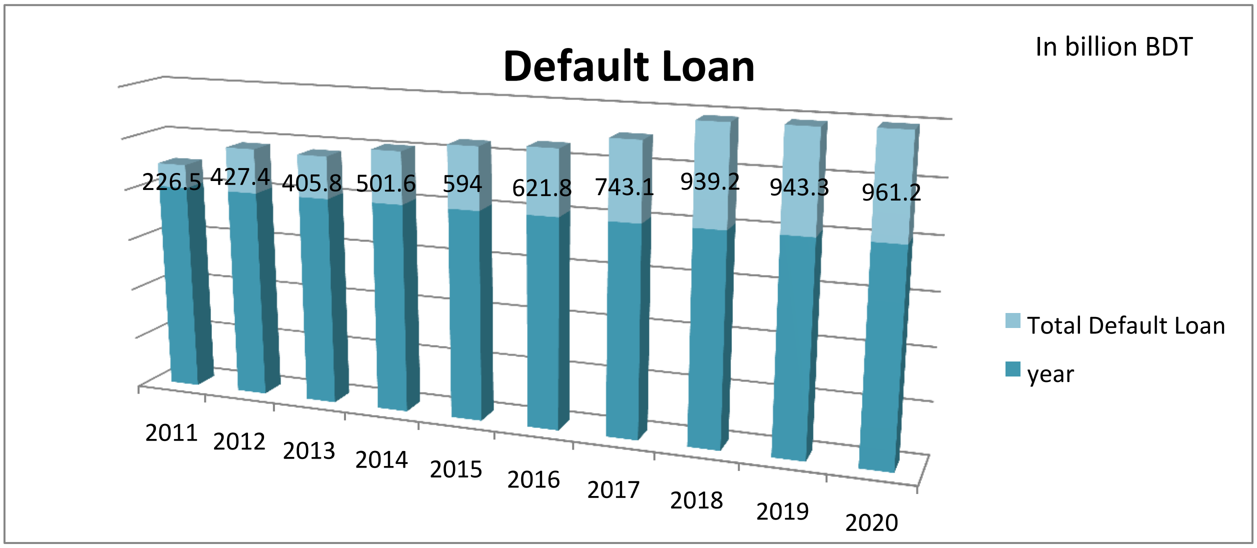


Figure -1.1 Source: Bangladesh Bank

Analyzing the effect of the defaulted loan in the emerging economy, then it can be seen-First, Lending Rates have been found to be not so significant in affecting the NPAs contrary to the general perception Bank Assets has turned out to be negatively significant indicating that large banks may have better risk management procedures and technology which definitely allows them to finish up with lower levels of NPAs. Second, private banks and foreign banks have advantages in terms of their efficiencies in better credit management in containing the NPAs that indicates that bank privatization can lead to better management of default risk. In the last ten years, the number of banks that were established in Bangladesh was not expected to increase their capacity to address the financial risk. And for the reason, that the country's banking system could not properly manage the Non-performing loan.

A non-performing loan is an important issue that can lead to increased unrest in the financial sector. If consider the Chinese market policies then see, "Chinese regulatory authorities have injected significant capital into the banking system and scrutinized NPLs since 2003. In addition increase in the NPL ratio raises riskier lending, potentially causing further deterioration of the loan quality and financial system instability".

PROFITABILITY:

Bank profitability is the **measure of a bank's performance**. Banks make a profit by earning or generating more money than what they are paying in expenses. The main part of the profit of a bank comes from the service fees, charged for its services and the earned interests from its assets.

1.2 DEFENATION OF TERMS

Bank:

A bank is a **financial institution where customers can save or borrow money**. Banks also invest money to build up their reserve of money. What they do is regulated by laws. Those laws differ in different countries. The people who work at a bank are called bank employees.

DEFAULT LOAN:

Loan default occurs when a borrower fails to pay back a debt according to the initial arrangement. In the case of most consumer **loans**, this means that successive payments have been missed over the course of weeks or months.

NON PERFORMING LOAN:

A non-performing loan is a loan which is either in default, or is about to be, with a reasonable expectation that the loan will enter default even though it has not technically defaulted yet.

BANK

1.3 OBJECTIVES OF THE STUDY

This study seeks to assess the effects of default loan on bank profitability in Bangladesh. What are the effects of default loan on the profitability of all banks in Bangladesh? Required specific objectives to examine the factors from borrowers of default loan that affect the profitability of all banks in Bangladesh. Finally, to provide recommendations to all types bank in Bangladesh on how to deal with loan default issues.

1.4 LIMITATION OF THE STUDY

We couldn’t evaluate the ratio of net NFLs to total loans (percent). Here we evaluate the total NPLs in amount with the ROA in percent. Because we can’t manage ratio of net NPLs data due to lack of budget and trustable source. If we can evaluate the ratio of net NPLs with the return on assets, it will more accurate findings than now. So it is the only limitation of this study.

Chapter: 02
Literature Review

2.1 The Concept of Loans, Loan Default and Default Loan Rate

A loan is usually available on a fixed and spot basis and can be secured or unsecured. Loans are offered for specified amounts for specified periods. In general, part of the major component of the total assets of every bank. The lender cannot seek repayment before the expiry of the period unless there has been some default. Default refers to a situation where a borrower failed to repay a loan. It occurs when a borrower cannot or will not repay the loan and the MFI no longer expects to receive payment. Technical default refers occurs when an affirmative or a negative covenant is violated and mainly applies to banks.

Default Loan Rate

Mohammad Ziaul and Mohammad Zakir (2018) undertaking a study on flawed interest rate policy and loan default note that, persistent loan defaults have become an order of the day in developing countries and this has had a serious negative effect in the development of financial market and economies of these countries. They further note that despite the application of a number of remedial measures, such as supplying fresh loans, loan rescheduling, imposition of penal interest rates, denial of additional credit to repeat defaulters, management takeover of problem projects, and legal actions, loan default problems continued to reign the credit markets in developing countries.

A high interest rate is one of the most important factors that influences borrower's ability to repay loans. It is widely reported (that high interest rates have devastating effect on investment and growth of an economy though McKinnon (1973) and Shaw (1973) underscored the importance of applying higher real interest rates during periods of inflationary pressure to promote savings and investment in financially repressed economies. Rotenberg (1991) found very high interest rates was detrimental to investment and growth. He recommended that interest rates should be kept low in order to speed the growth of investment and economy at large. The virtues of low interest rates are: it will increase borrowing, reduce inflation, increase job opportunities and stimulate the national economy.

A study on inflation on long term housing loans, notes that the extension of long-term loans, for example to finance housing, is adversely affected by inflation. Banks charge higher nominal rates in response to inflation which means that 21 borrowers have to make (nominally) higher interest payments, which unnecessarily reduces their borrowing capacity. Long-term loans with variable interest rates increase the probability that borrowers will become unable to meet their payment obligations.

Hoque and Hossain (2008) observe that a high interest rate cause inflation which increases the cost of production or costs of goods sold. Such cost escalation can reduce Earnings before Interest and Taxes (EBIT). Additionally, the interest expense may not be covered by the EBIT which means that nothing is left for loan repayments. This means, high interest rates may end up with higher liabilities and if liabilities are greater than assets, borrowers will not be able to repay loans and hence, debt default occurs

Hoque (2004) notes that banks do charge high interest rates in developing countries where the financial market is imperfect due to the prevailing information asymmetry between borrower and lender, doubtful credit-worthiness of borrowers, overstated value of collaterals and inefficiency is the common features at institutional level. Nobody knows the precise degree of such imperfection but all banks are addicted to the policy of high interest rates, a move he concludes to be counterproductive as high interest rates may contribute to loan default. He further suggests that banks should determine appropriate lending rates on the basis of proven, not hypothetical, degree of market imperfection.

Roe (1982) suggested that real rate of interest must be lower than real return on capital. It means that as the financial market becomes more and more efficient as development occurs, lending rates should be lowered than before which may contribute towards reduced level of loan defaults. Failure to do this may result in persistent loan defaults in developing countries. Rittenberg (1991) has identical findings that high interest rates can be detrimental to investment and growth. High interest rates do not contribute to banks growing profitability in the long run. Stiglitz and Weiss (2004) believe that high rates are responsible for higher defaults and declining bank profit. Again, lending rates should be lowered or adjusted very frequently with the level of real-world imperfection which decreases with pace of economic development and growth of an economy.

A World Bank (1995) report on non-performing loans in Bangladesh banks noted that a total of 40% loans were non performing. It required a spread of 20% between lending rates and bank's cost of funds just to break-even. Owing to the existence of a large number of non-performing firms as well as high default rates, banks in Bangladesh resorted to high lending rates which, again, compounded the default rate. In this way, banks were caught in the vicious circle of high interest rate and high loan default rate. This reinforces the point that a higher interest rate is positively related to a higher incidence of loan default.

The study further observed that a high interest rate was one of the contributing factors to loan default in the industrial sector, particularly in the manufacturing sector in the country. This suggests that loan default could not solely be attributed to borrowers' unwillingness to repay loans; it was also an inbuilt problem of the interest rate policy. In other words, the interest rate policy was both a cause and an effect of the high loan default rate in Bangladesh (Hoque 1998 and 1999c). As high interest rates increase costs of borrowing, debt burden grows which leads borrowers to default and, as loan default becomes persistent, the banks lose income and becomes undercapitalized. In order to recover its financial position, it resorts to high interest rates and the cycle is complete. The borrowers are to bear the brunt of this inconsistent interest rate policy. All these indicate that high interest policy pursued by the banks in Bangladesh worked as one of the contributing factors for industrial loan default.

This chapter reviewed the empirical and theoretical work brought out by different researchers in relation to inflation, commercial bank lending volumes, lending rate and default rate. Similar studies carried out in different economies revealed different response with most of the studies showing strong relationship between the macroeconomics variables understudy while others gave a contrary opinion.

The discussion was broken down into various specific objectives with a discussion on what other studies have found on the effects of inflation on other lending parameters such as base lending rate, lending volumes and rate of loan defaulting was done.

However, in-depth study on the effects of inflation in commercial banks' lending in Bangladesh with a specific focus of Bangladesh commercial banks was not looked at in this literature review; hence the purpose of this study so as to close this gap. The following chapter dwelt on the research methodology which was used to determine the effects of inflation on commercial bank's lending in Bangladesh

2.2 Non-Performing Loans

According to Fofac (2015) loan is considered non-performing when payment of interest or the principal amount is past due by ninety days or more or interest payments equal to ninety days or more have been capitalized and such a debtor show no indication of fulfilling his pledge of payment or has even filed for bankruptcy. These loans remained classified as such until written off instruction is issued or payments of interest and /or principal are received or subsequent loans that replace the original loan issued.

Fofac (2015) notes that Non-Performing Loans leads to a reduction of liquidity in banks and thus its credits expansion and as results affecting the overall performance of the bank. There is also increased liquidity risk and credit risk, she further notes that the due to the nature of banking business commercial banks expose themselves to loan defaulters from borrowers, hence prudent risk assessment strategies and adequate provisions need to be put in place to cushion banks risks, and thus when the level of non- performing loans are high provision may not sufficiently offer cover for protection.

Undertaking a study on the determinants of non-performing loans in Sub Saharan Africa using correlation and causality analysis note from the analysis data from sixteen sub-Saharan countries. The sample selection was chosen based on the availability and the database of financial information on these countries. At the macroeconomic level, 19 the study investigated the correlation between non-performing loans and a subset of economic variables: inflation, interest rates, and changes in the real exchange rate, interest rate spread, per capita Gross Domestic Product and broad money supply. At the microeconomic level, it focuses on the association between nonperforming loans (NPLs) and banking-sector variables. The key banking variables include return on asset and equity, net interest margins and net income, and inter-bank loans. These variables were chosen in the light of theoretical considerations and subject to data availability. Nonperforming Loans (NPLs) were adjusted for specific provisions (non-performing loans as a proportion of loans loss provisions) to provide the basis for cross-country comparisons.

In the correlation analysis, the results showed a negative association between real GDP per capita and non-performing loans expressed as a percentage of loans loss provision. This implies that falling per capita income is associated with rising scope of Nonperforming Loans (NPLs) to the extent that changes in per capita income is proxy for changes in economic growth. The negative association with nonperforming loans indicating the impact of cyclical output downturns on the banking sector.

A study on how ownership structure affects Non-Performing Loans (NPLs) notes an increase in government's shareholding in an organization encourages political lobbying whereas private shareholding induces more Non-Performing Loans (NPLs) which are manipulated by corrupt private owners the finding showed that the rate of NPLs decreased as the ratio of government shareholding in a bank rose to a figure of 63.51%, while the rate thereafter increased. A joint ownership between government and private shareholding had the lowest rate of NPLs.

According to Khemraj and Pasha (2009), examining the factors causing non-performing loans in Guyana Commercial bank for the period between 1994 to 2004, noted that real growth in Gross Domestic Product (GDP), real effective exchange rate, and real interest rate significantly impacted the non-performing loans. Dash and Kabra (2010) investigating the association between nonperforming loans and banks specific variables macroeconomic variables in India, noted that the real effective exchange rate, real interest rate, the bank size and real interest rate, the bank size and real GDP related with NPLs while inflation rate was found not be useful in their study

2.3 Factors leading to Loan Default

So many researches have focused on what causes loan default and so to say there are few reasons would be an understatement, but the following reasons can be advanced for in the case of this study.

i. Loan supervision: Recent studies into loan default have pointed out that most cases of default happen as a result of inadequate supervision from loan officers and supervisors when loans are granted to clients. This aspect has caused the tendency for default to increase dramatically in the past decades.

ii. Monitoring and control: At times, when loans are granted to customers, they are not monitored as to be used for what they were intended for and as such there exist no control and this turns to increase the rate of default in institutions involved in credit provision.

iii. Grace Period: Several lending practices showed that grace periods have been too short to serve their intended purposes. Especially this can be left in the start-up phase of the business. The grace period also affects the repayments of loans although it is intended to protect the lending institution.

iv. Insider Lending: According to Brown Bridge (1998), bad loans accounted for most banks which were in distress and the major causes of these bad loans were insider lending, macro-economic instability and lending to the high-risk borrower. Insider lending was identified as one main factor of bad loans that led to the collapse of local banks. Ahmad, (1997), mentioned some important factors that cause loan defaults, which include:

v. Voluntary unwillingness to pay: Lack of willingness to pay loans coupled with the diversion of funds by borrowers.

vi. There is willful negligence and improper appraisal by Credit Officers.

vii. Also, Hurt and Fesolvalyi (1998), cited by Kwakwa, (2009) found that, corporate loan default increases as real gross domestic product decline, and that the exchange rate depreciation directly affects the repayment ability of borrowers.

2.4 Effects of Loan Default

Default loans cost a lot on a bank on the way of its progress.

i. Diminishes Asset Quality: Default loan diminishes the asset quality of a bank. Loans are the assets for a bank. When a loan becomes default, the asset loses its value and become a liability. This decreases the total asset amount of a bank.

ii. Increases the Cost of Funds: For NPL, banks have to maintain some provisions for ensuring the future payments of the depositors. This increases the cost of fund of the bank.

iii. Decreases the Profitability of the Bank: If a bank cannot manage to get a loan repaid, it becomes bad debt. The bank still has to repay the depositors when they demand to withdraw their money.

In this case, the bank needs to pay the deposited amount from its profit, which decreases the total profit of the bank.

iv. Decreases the Overall Credit Rating of the Bank: If a bank cannot manage to collect its loan amounts it will face a tremendous problem as it will lose its credibility to repay the depositors properly, moreover, its profit will decrease continuously. It will face challenges to do business with foreign banks. All of which will lead to the poor credit rating of the bank.

v. Decrease the Capacity of Loan Sanctioning: When a loan becomes non-performing, provisions are to be kept against the said loan; as a result, the option of farther sanctioning loan hampered since the provision to be kept from the profit portion which could be farther invested by keeping retained earnings.

2.5 Measurement of Bank Profitability

To determine the profitability of banks, simply looking at the earnings per share isn't quite enough. It's also important to know how efficiently a bank is using its assets and equity to generate profits. Financial statements of banks demonstrate some ratios and some can be calculated based on requirements if needed. Koch and MacDonald stated that relatively appropriate measures for measuring the bank`s profitability level are Return on Assets (ROA) and Return on Equity (ROE) and also Net Interest Margin. This study focuses on ROA.

Return on Assets (ROA)

ROA is calculated as a percentage of net income and total assets. ROA is used as main profitability measure in most of the organizations including banks and financial institutions. It demonstrates the level of net income produced by the bank and also determines how the assets utilized by banks to generate profit over the years. The competence and proficiency of banks in transforming their assets into profits is also indicated by it. Hence, to improve the performance of banks, they always attempt to achieve higher ROA. The ranking of banks is usually based upon the higher ROA ratio and total assets. As a general view, particularly in the banking sector, ROA is known as good profitability multiplier for the reason that equity multiplier does not influence it.

Equation 1: Return on Assets Equation

$$Return\ on\ Assets = \frac{Net\ Income}{\text{Total Assets}}$$

2.6 Relationship between Loan Default and Bank`s Profitability

Briefly, the process of banking is to collect idle money and invest this money in the economy. In this process, one party who has the idle money deposits in a bank and the other party who needs the money borrowed from the bank. The depositors get some interest on their deposited money and the borrowers pay some interest payment on the amount of money they borrowed. Bank has no money of its own, it just works as an intermediary between two parties, and so if the borrower cannot pay the money back to the bank, the bank must repay the money to the depositors from bank's profit. Therefore, there is always a risk in loans if the loan will be repaid to the bank or not. Page 8 of 24 It will be fallacious to say that when loan default happens, banks do not witness a dramatic fall in their operations; this is because: First, the amount of money in their possession meant for borrowing reduces, secondly their interest, in turn, reduces, as they can no longer borrow, furthermore, they witness a drop in finances further as they have got to pay back interest to depositors and they have to do this from their profits. Without enough finances and profits, their whole operation starts to break down and we see to certain extent banks declaring insolvency and bankruptcy.

2.7 Impact of Default Loan on Bank profitability

Bad **loans** arise when the borrower no longer pays in accordance with the terms of the **loan**. This has a negative **impact** the **bank**'**s profitability**, can lead to credit losses and, at worst, **default**. Put simply, large volumes of bad **loans** risk reducing bank equity, making it more difficult to issue new **loans**. Adequate management of bad **loans** involves banks identifying such **loans** at an early stage and writing down the value of them equal to the expected credit losses. For **unprofitable** banks, this leads to a reduction in their equity. Following the latest crisis period, many European banks have not had sufficient equity in order to correctly manage their bad loans. This has led to major uncertainty regarding banks' viability, i.e. whether they have sufficient equity to be able to survive in the long term. In several European countries, neither regulation nor banking supervision has been sufficiently strict, which has allowed many banks to neglect fully dealing with their bad loans. This has severely exacerbated the difficulties involved in reducing the volumes of bad loans in Europe.

2.8 Total scenario of Default Loan in Bangladesh and Among the Developing Countries

The actual size of bad loans is more than double the officially recognized figure, according to a recent report of the International Monetary Fund -- a damning evidence of the fragile state of Bangladesh's banking sector. At the end of June 2021, the banking sector's total defaulted loans stood at Tk 112,425 crore, which is 11.69 percent of the total outstanding loans, according to BB data. The amount of NPLs increased to taka 961.2 billion in 2020 from taka 47.3 billion in 2003.There are many reasons behind the NPLs in Bangladesh. First reason is entrepreneurs related. Borrower may be have lack of experience, lack of business and lack of institutional training background or lack of supporting facility. Sometime borrowers do it intentionally. Entrepreneurs age also an important factor. Second reason is business related. Sometime banks give loan to businesses which are not attractive. Strong competition is another business related cause. Borrower becomes defaulter if there is poor management capability, poor financial performance, and poor cash flow. Business could be defaulter because of low market share. Low market share mean low revenue so that business cannot pay the interest payment. Third reason is leading related.

It is mainly Bank's fault. Loan could be default if Bank delayed assessment of loan proposal, delayed disbursement of fund, lack of proper monitoring, lack of taking proper action. Last reason is macroeconomic factors. Low GDP growth, increasing crimes, hurtles and frequent policy change effect loan. For those reasons loans become default loan. Effects of NPL are such as Stopping Money Cycling, Earning Reduction, Capital Erosion, Increase in Loan Pricing, Frustration etc. As a result, the values of security are increased and the risks of financial recession also see a rise.

The biggest problem is the absence of good governance in the banking sector of Bangladesh, which is not possible to take action altogether. Two factors can be identified as a reason for the increase in Nonperforming loans. First, the bank's directors aggressively take a loan from his own bank as well as another bank. In this issue quoted from Financial Express, "Bank directors are taking loans from their own banks as well as from other banks. Directors of 19 banks have taken loans of Tk 4.00 billion from their own banks. Directors of nine banks have given loans of Tk 2.31 billion against their personal guarantee." Second, getting more bank in the economy and expressing their inefficiency. Another quote from

Financial Express revealed that "Among these banks, Farmers Bank had the highest default, Tk3.78 billion, at the end of September, 20 17. The financial situation of this bank is deteriorating fast. On the one hand, loans are not being repaid and on the other, sufficient deposits are not coming. The bank is not in a position to return the money of the depositors. NRB Commercial Bank is second in respect of loan default. Their default amount is Tk1.94 billion. Meghan Bank is third on the list of defaulters. Their default loan amounts toTk1.52 billion. Midland Bank has a default of Tk460 million. South Bangla Agricultural Bank's default is Tk150 million and Modumoti Bank has a default of Tk14 million. The country tops the list of loan default index in South Asia. Bangladesh's default loan ratio was estimated at 11.4 per cent for 2019 in the World Bank's latest 'Global Economic Prospects' report. It portrays the squandering culture of public money in the name of borrowing from the banking sector.

The contemporary banking crises are not accompanied by declines in aggregate bank deposits, and credit does not fall relative to output, but the growth of both deposits and credit does slow down substantially. In the case of credit growth, stronger banks reallocate their asset portfolio away from loans. This suggests that protecting deposits during a banking crisis may not be enough to protect bank credit, as lack of usable collateral and poor borrower creditworthiness discourage banks from lending. However, protecting bank credit may not be a priority right after a crisis, as the real economy can rebind without it, at least while there is substantial underused capacity.

Among the developed countries, Pakistan has the highest amount of nonperforming loan that is 9.2%. In this situation, India and Bangladesh are almost equal, in terms of law enforcement; the neighboring country is very much ahead. Recently the Indian government has approved the law namely „the Economic Offenders Bill 2018‟ to prevent nonperforming loan. For instance, If anybody is involved in the loan default, all his accounts will be seized. In China, there is a passport blacklist process. Unfortunately, there is no punishment for closing down the defaulted loan in Bangladesh, there are weaknesses in law enactment also. Below is a picture of the default loan scenario in recent times.

Chapter: 03
Research Methodology

RESEARCH METHODOLOGY

This chapter provides a discussion of the research methodology that was used in this study. It discussed the research design especially with respect to the choice of the design. It also discusses the Banks of study, sample and sampling techniques, data collection methods as well as data analysis and data presentation methods employed in the study.

3.1 Research Design

The study adopted descriptive research design. Descriptive studies attempt to describe a subject by creating a profile of a problems, Banks, or event while explanatory studies attempt to explain the reasons for the phenomenon that descriptive study only observed. The study used a descriptive design because it enables the researcher to collect in-depth information about the Banks being studied. The descriptive design gave proper and succinct recommendations to the management of Banks

3.2 Sampling Technique

The choice of sampling period was based on the availability of time series data on new volumes of Default Loan by Banks as well as the availability of ROA. The study used time series data for ten years from 2011 to 2020. The ten-year period data will be enough to provide the researcher with desired results. The period has also been purposively determined since it is the most recent period for the study.

3.3 Data Collection Methods

The study secondary data. Secondary data on bank default loan volumes, Default Loan and bank Return on Assets were obtained from administrative records and documentation while data on Default Loan was obtained from the Bangladesh Bank for a period of Ten years between 2011 to 2020. Through this method, the researcher was able to obtain information on Banks perceptions on the effects of Default Loan on the Bank Profitability.

3.4 Data Analysis Methods

This study used the quantitative method of data analysis. To ensure easy analysis, the questionnaire was coded according to each variable of the study to ensure the margin of 27 errors is minimized to assure accuracy during analysis. The quantitative analysis was applied using descriptive and inferential statistics.

The secondary data was analyzed using simple Linear Regression analysis model. Two variables can have a linear relation captured using the formula $Y = \alpha + \beta(X) + \mu$; where α is the constant β intercept or slope and μ the error term. Regression and correlation analysis shows us how to come up with both the strength and the nature of the two variables. Hence the giving us the relationship between variables. The known variable is called the independent variables (x) which include the Default Loan volumes.

The unknown variable that is estimated depending on the objective being sought from the research questions that was Default Loan volumes. A scatter diagram is drawn for the case of regression analysis ,the regression line is put in place by fitting the lines visually among data points ,whereas the correlations analysis was also used to describe the degree at one variable is linearly related to the other.

Coefficient of determination was also used to give the extend, or the strength of the associations between two variables X and Y. A sample coefficient of determination was developed from the relationship between two kinds of variations that is a sum of group of squared variations. The variations of the Y values in a data set around the fitted regression line and their own mean.

Regression can be bivariate (between 2 variables, x and y) or multivariate between greater than two variables, both have been used in the study, with objective one and three using bivariate whereas objective two using multivariate approach.

3.5 Relationship between Default Loan and Bangladesh Banks Return on Assets (ROA) from the year 2011 to 2020

In order to establish the effect of Default Loan, graphs were used to illustrate the trends. The Annual Return on Assets for the period 2011 – 2020 were regressed against the banks Default Loan. The linear relationship between the dependent variable in this case, the commercial banks' lending rate and the independent variable s being inflation were generated. A simple regression was used for regression analysis and inferences were drawn based on the regression analysis.

Thus, given that

BR=Default

Loan IR =

Inflation Rate

$\alpha 3$ = Constant

$\beta 3$ = Slope

/Intercept

$\mu 3$ = Error term

The following linear equation is generated:

$$BR = \alpha 3 + \beta 3 (IR) + \mu 3$$

Chapter: 04 Findings and Result

Assess to Impact of Default Loan on Profitability

The results are mainly presented using regression analysis, frequency tables and charts. The results are mainly presented using regression analysis, frequency tables and charts.

First, General Information that covers the general characteristics
Secondly, Research Question 1: Correlation relationship between Default Loan and Return on Assets.
Finally, Research Question 2: Regression analysis between Default Loan and Return on Assets.

4.1 Bangladesh Default Loan Volumes 2011-2020

Table 4.1 indicates the Default Loan from June 2011 to June 2020 in billion BDT.

YEAR	DEFAULT LOAN
2011	226.5
2012	427.4
2013	405.8
2014	501.6
2015	594.0
2016	621.8
2017	743.1
2018	939.2
2019	943.3
2020	962.2

Tabe-1 source: Bangladesh Bank

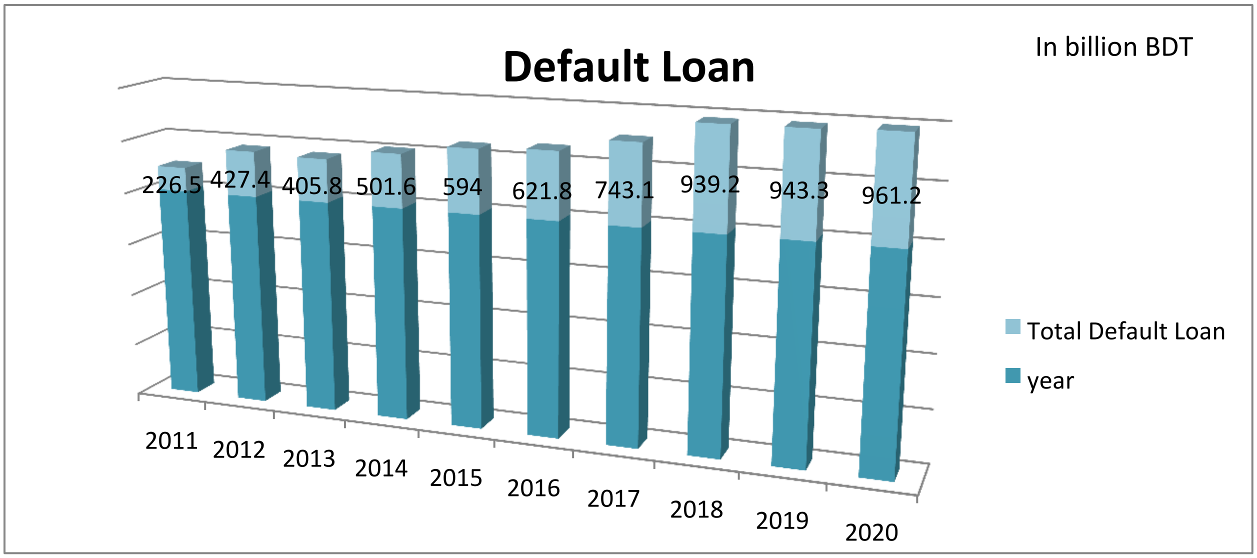


Figure 4.1: Trends in Default, 2011-2020

4.2 Return on Assets 2011 to 2020

Table 4.1 indicates the Return on Assets from June 2011 to June 2020 in percent.

YEAR	RETURN ON ASSETS
2011	1.5
2012	.64
2013	.90
2014	.64
2015	.77
2016	.68
2017	.74
2018	.25
2019	.43
2020	.42

Tabe-2 source: Bangladesh Bank

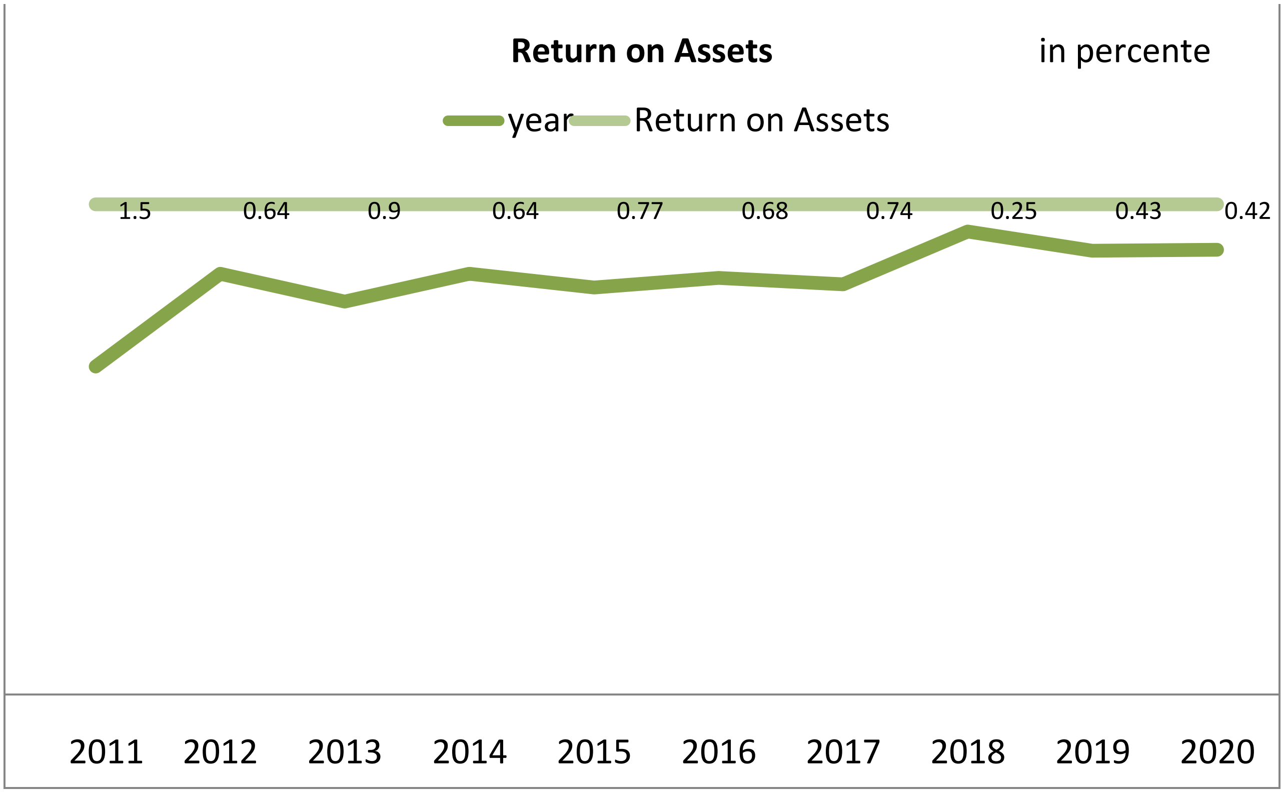


Figure 4.2 Trends in Return on Assets, 2011-20

4.3 Correlation between Default Loan and Return on Assets (ROA)

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Default Loan	226.5	427.4	405.8	501.6	594	621.8	743.1	939.2	943.3	961.2
Return on Assets	1.5	0.64	0.9	0.64	0.77	0.68	0.74	0.25	0.43	0.42
Correlation	-0.8434									

This calculation using Microsoft Excel

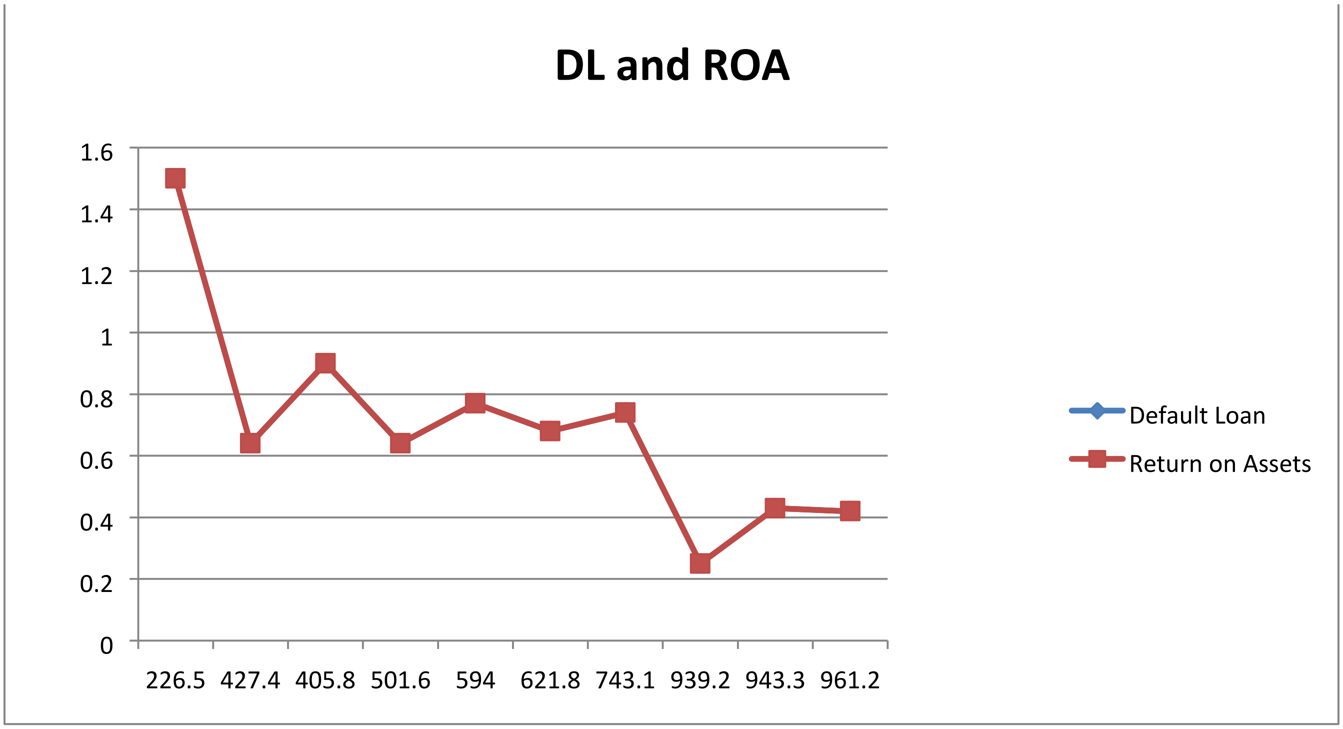
4.4 Regression Analysis of Return on Assets (ROA) on Default Loan

SUMMARY OUTPUT								
Regression Statistics								
Multiple R	0.84337999							
R Square	0.711289808							
Adjusted R Square	-1.25							
Standard Error	0.19445868							
Observations	1							
ANOVA								
	df	*SS*	*MS*	*F*	*Significance F*			
Regression	10	0.745296574	0.074529657	19.70945	#NUM!			
Residual	8	0.302513426	0.037814178					
Total	18	1.04781						
	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept							0	0
Default Loan							-2.4631E-306	2.4631E-306

226.5							65535	65535
427.4							-2.292E-268	2.292E-268
405.8							65535	65535
501.6							-2.8736E-306	2.8736E-306
594							65535	65535
621.8							0	0
743.1							-6.9654E-239	6.9654E-239
939.2	1.413586172	0.172727232	8.183921857	3.71E-05	1.01527646	1.811895884	1.01527646	1.811895884
943.3	-0.001126017	0.000253634	-4.439532386	0.002169	-0.001710899	-0.000541136	-0.001710899	-0.000541136
961.2								

This calculation using Microsoft Excel

The study further suggests that Default Loan has strongly effects on the Banks Profitability since as Default Loan increase; strongly effect is exerted on Banks Profitability.



DL and ROA
1.6
1.4
1.2
1
0.8
0.6
0.4
0.2
0
226.5
427.4
405.8
501.6
594
621.8
743.1
939.2
943.3
961.2
Default Loan
Return on Assets

Chapter: 05
Recommendations and Conclusion

5.1 Recommendations

- In order to reduce the defaulted loan in Bangladesh, good governance in the banking sector is very much needed for instance banking must stop the family business and there should be strict monitoring cell to observe loan recovery system.
- There should be proper rules for an appointment and cancel the bank's director. In this case, the government and the Bangladesh Bank must have the authority to observe this issue.
- There should be proper policies and surveillance in the evaluation of the performance of the Fourth Generation Banking.
- Basically, Non-performing loans are affected by the capital to risk-weighted assets ratio (CRAR). so this will work to improve the quality of the CRAR and
- Mandatorily to implement Basel III guidelines alongside prudent implementation of the banking law for all banks.

5.2 Conclusion

Default loan (Non-performing) culture has been found in different countries of the world, in Bangladesh, this problem has become apparent in the last few years. Structural weakness, political will and lack of good governance are main factors for the bank industry depressed. There may also be a reason for the small economy to move more to the bank.

In order to overcome this situation, the family tradition in banking will be reduced in the bank sector in the country, at the same time, the capacity of the country's central bank to increase immediately. As the goal in front of Bangladesh is to become a developed country by 2041. Before that, one of the main goals is to achieve SDG by 2030.

The 16th goal of the SDG‟s seventeen goals is being „Peace, justice, and strong institutions‟. Making banks a strong institution, to ensure peace and justice at the stakeholder level.

References

Central Bank of Bangladesh (BB) (2019-2020), Annual report.