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Research Article

Corporate Governance and Non-Performing Loans: A Study on Commercial Banks in Bangladesh

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Abstract

This study attempts to identify the challenges to reducing Non-performing loans (NPLs) by means of implementing proper corporate governance practices in an effective manner in Bangladeshi banking sector. Corporate governance ensures practice of ethical standard in workplace, ensures discipline, sincerity and dedication of employees and thus ensures the productivity of the organization. Corporate Governance issues like Board size, composition of Board of Directors (BoDs), board committees, governance practice etc. in banks having different assets size, business volume, customer base and ownership pattern have been compared to draw a comprehensive conclusion regarding the effects of corporate governance in controlling the NPLs in banks. The findings show that, there exists a positive relationship between assets size and NPL, Advance Deposit Ratio (ADR) and NPL, size of board and NPL. But there are few issues like presence of Independent directors in board, role of Audit committee (AC) and Risk management committee (RMC) at board level etc. which are inversely related with the scenario of NPL. The data have been collected from different banking and financial sources including Bangladesh Bank (BB) - the central bank of the country and cover the entire banking industry including state owned, private and foreign commercial banks. A trend analysis of the previous periods and the corresponding changes of NPLs over the years have been analyzed in relation to the corporate governance variables to derive results and get an insight regarding the corporate governance practices and the impact of it in management of NPLs with respect to supervision, compliance and monitoring from both on and off site locations inside the bank and at central bank level.

Keywords: NPLs-Non Performing Loans; ADR: Advance Deposit Ratio; BB: Bangladesh Bank; RMC-Risk Management Committee; AC- Audit committee (AC); Bo Ds: Board of Directors

Introduction

In Bangladesh, Banking sector has already passed more than 50 years in operation. The sector started with the limited number of banks in 1972 now comprises more than 60 banks. It is highly competitive and sensitive industry with liability mostly taken from depositors and other investors'. Thus regulatory bodies need to be responsible and responsive to ensure and protect the interest of the depositors and investors by means of effective operation of the banking sector. Fall of few banks in early 90s and in the early 2000's, central bank made cautious move in banking sector operation and enacted few rules, regulations, and policies to enhance control mechanism and supervision authority.

NPLs in the banking sector have been an area of concern for regulatory authorities, banks, governments with relation to its negative consequences in the banking industry, financial sector and in economy of the country. Increase of NPLs creates obstruction in credit growth because of cautious and defensive credit program of the banks which in turn affects entrepreneurship development, employment generation, production functions, economic functions and above all contribution of financial sectors as well as manufacturing sectors to the GDP growth of the country. It is observed in the past days that increase of NPLs in the portfolio exposes banks towards a significant risk and thus discourages lending by banks because of risks of default and loss of investment (the fund disbursed) as it pushes the provisioning requirement, capital erosion and reduces the profitability of the bank and even hinder the smooth operation of the banks.

In order to address these consequences regulator has taken stringent measures for strengthening corporate governance in banks by enacting regulations regarding the formation of corporate culture, board size, structure, nature and responsibility to ensure governance and monitoring at the top. Although the effectiveness of the governance framework and governance structure is questionable, it might bring fruitful outcome for banks in the long run and bring about a change in banking operations. This paper investigates relationship between two parameters-Non performing loans and corporate governance-of the local commercial banks in Bangladesh. By understanding the nature and extent of gap in performance between corporate governance and NPLs, this study attempts to identify the drawbacks to reducing NPLs by means of implementing corporate governance effectively in Bangladesh's banking industry.

For banking sector, being a leveraged institution, discipline, accountability, responsibility and transparency are indispensible. Corporate governance also ensures a check and balance in the activities of the entire organization from top level to the bottom. Taking such aspects into consideration and to address negative consequences of banks like the NPLs, regulator has taken stringent measures for strengthening corporate governance in banks by enacting regulations regarding the formation of corporate culture, board size & structure, board compositions, nature and responsibility of board of directors to ensure governance and monitoring at the top. This article is completely conducted on secondary sources of data and the study is descriptive in nature.

Concepts of NPL and Corporate governance

NPLs refer to assets that give banks irregular installment payments and/or interest earnings. NPL ceases to "perform" and reduces income for the bank. Loan is the main source of earnings and cash inflows for banks because banks make profits from the loan repayment received in the form of interest earnings.

Credit is thus an integral part in banking business and considered as the prime earning source for banks. Of the total assets in the balance sheet of banks, loans and advances comprise almost 55% to 60%. (As shown in Table 1). Credits are the major earning components of bank portfolio that covers almost 50% of the total interest income that bank earns from its various operational activities (Of the total income interest income contributes the royal part and of the total interest income major earnings come from loans). As banks are exposed to credit facilities they get exposed to risks of various dimensions including default risk of borrower or migration risk of credit quality of borrower by means of deterioration in credit grading.

Table 1: Asset Structure of the Banking Industry (Amount in billion BDT).

Property and Assets	30-09-2016	31-12-2016	31-03-2017	30-06-2017
Investment	2154.9	2148.6	2055.4	1942.5
Loans and Advances	6736.4	7136.5	7370.4	7775.7
Fixed Assets	225.8	224.7	224.9	225.8
Other Assets	867.1	687.3	687	760.1
Total Assets	11,296.60	11,625.30	11,781.10	12,370.30
Source: Bangladesh Bank (2017)				

During last few decades and particularly in recent years, increase of NPL has reached in an alarming situation and has become a major threat for the banking business as shown in Table 1. Trend of such increase in NPL caused because of factors like- deficiency in proper appraisal system, absence of expertise among employees, unavailability of data, poor management, lack of corporate governance in the ownership of banks, lack of monitoring and supervision from both bank and supervisory level etc.

Table 2: Trends of Amount of NPLs of banks (Billion BDT).

Year	2009	2010	2011	2012	2013	2014	2015	2016	Jun-17
Amount of NPLs	224.8	227.1	226.4	427.3	405.8	501.6	594.1	621.8	741.5
Source: Bangladesh Bank (2017)									

The effects of NPL have become massive in relation to profitability, liquidity management, capital management and overall performance of the bank. In recent times few banks faced liquidity crisis, capital shortfall, government and regulatory intervention and reform for failing in maintaining effective operation and regulatory compliance. Considering such effects of NPL, Bangladesh bank has designed a regulatory framework to strengthen the capability, involvement, responsibility, monitoring and accountability of Board of Directors to ensure corporate governance, risk management, and smooth operation of the bank.

As part of monitoring devises and to ensure corporate governance in banks, Bangladesh Bank has provided a framework regarding formation of Board and its committees as well as the responsibilities (Terms of Reference) of all these segments in regard to policy formulation, review of policies, effective monitoring and control system in day to day banking operations.

Bangladesh bank has instructed the banks to form few committees within the board of directors comprising few members to ensure board level monitoring in relation to proper management of banking activities and to bring a change in corporate culture, management prudence, monitoring activities, risk management, management accountability, transparency in operations and sustainability of banks in the long run.

Literature Review

Corporate governance refers to the laws, regulations and business practices that together govern the organization and establish the relationship between corporate managers and entrepreneurs [1]. According to (BCBS) (2006) [2], corporate governance practices in the banking system should act in an effective manner for achievement of trust and confidence of public as well as for proper functioning of the banking sector. (BCBS) (2006) [2], also outlined that practices of corporate governance in an effective manner for proper and smooth functioning of banking in particular and economy as a whole.

With respect to economic perspective, there is a significant role that corporate governance can play to achieve efficiency where funds are transferred to investment that brings higher returns. It has also become an important factor in case of investments at institutional level [3] and elements of reform initiatives for institutional investors' [4].

The board size implies the number of directors constituting banks board [5-6] suggests that board size include the executive and independent directors [7]. Goshi et al. (2002) [7]. Also mentioned that on an average sixteen directors could constitute an optimal board for bigger companies

Having inside and outside directors in board have both merits and demerits in terms of performance and efficiency of the organization. But Outside directors can play superior rule because of separation and freedom from management [8]. Directors from outside of the business can contribute in board's strategic decision-making and supervision of the management and thus enhance the function and effectiveness of board [9].

Altunbas et al. (2000) [10], after performing analysis regarding efficiency of banking in consideration of cost efficiency during 1993 to 1996 in Japan, shown that non-performing loans are positively related to bank inefficiency.

According to Siamat (2005: 174) [11] NPLs may be termed as an infrequent repayment from borrower because of existence of gaps or external factors which are uncontrollable in nature from the borrower's perspective.

Large board size usually enhances performance. But some argue that board with large size is unlikely to function in effective way (Jensen, M.C. 1993) [9] and could reduce individual responsibility and increase involvement in bureaucratic problems.

Adams and Ferreira (2009) [12] did not find any relationship between the presence of independent directors in board and the performance of the organization; outside directors in board play a positive role, Kaplan and Minton (1994) [13]. Recent studies state that director independence do not capture social relations that may impair a directors judgment in monitoring (Cohen, Frazz- ini and Malloy, 2009; Hwang and Kim, 2008) [14, 15].

According to Siamat (2005) [11] NPL ratio can be used to determine potential bad debts and High NPL ratio indicates inefficiency of bank and its management in managing the assets. The Good Corporate Governance application at bank is expected to reduce the inefficiency and/or fraud in lending and has impact on NPL.

As stated by Aziz et al. (2009) [16] the rising of non-performing loans (NPLs) affects the lending function of banks, tighten lending and switch the attentions for management of NPLs in balance sheet. This reduced funds to deploy in earning activities. Higher non-performing loan also affect the bank's profitability, causes capital erosion and hinders sustainability of bank.

Waweru and Kalami (2009) [17] stated that commercial banks usually get exposed to different risk factors for the business nature. NPLs is not at all new for banks rather it began in early 1980s at the time government started expansion of policies on credit and infrastructure for banking along with lack of expertise on the other [18].Families and kin can influence the rational decision making of the organization, Uddin and Choudhury (2008) [19].

Research gap: Although corporate governance has been widely discussed, written and presented in different articles and papers, it is observed very few of those could relate the impact of it on NPLs directly. NPLs, in some articles, have been a part or parameter of the analysis used to determine corporate governance practices but no specific analysis being performed by establishing a direct relationship was absent in the materials reviewed so far. Considering such aspect, endeavor has been taken to produce the NPL directly relating with the corporate governance in the banking sector of Bangladesh.

Objectives

The main objectives of this study are as follows

1. To see the current state of corporate governance in the banking sector
2. To review the regulatory reforms relating to corporate governance for management of NPL
3. To exhibit the practice of corporate governance in commercial banks
4. To analyze impact of governance on Non-Performing

loans of banks

5. To suggest few recommendations based on study findings.

Methodology

The study has been performed to examine the corporate governance practices of banks in Bangladesh and to observe the effects of corporate governance of the banks in management of non-performing loans. The study has been conducted based on 08 years data (2009-2017) of commercial banks in Bangladesh and data have been collected only from secondary sources including websites of the respective banks, library of Bangladesh bank, BIBM and different banks etc. Finally data were analyzed based on the qualitative judgment; trend analysis of performance over the years and the present state of financial stability in banking industry in relation to NPLs management to supplement findings and arrive at a meaningful conclusion. The study is basically qualitative and explanatory. The analysis of the report has been performed considering a number of dimensions relating to corporate governance including board size, ownership pattern, govt. nominated directors in board, independent/non-executive directors, meeting of audit committee, risk management committee, total assets size, Total Loans, ADR etc. and compared with the trend of NPLs of banks during 2009--2016 i.e. comparison of the situations before and after the practice of corporate governance (Up to 2013 and then new governance regulations from 2013 to onwards). In this study, impact of corporate governance aspects has been portrayed over NPLs.

Overview on NPL and corporate governance Regulations (Global and Domestic)

The financial sector of Bangladesh comprises of banking sector and capital market. The capital based financial sector is yet to get its full pace functioning. Rather the banking sector is comparatively developed, disciplined, and reliable due to stringent monitoring by regulator (Bangladesh Bank). Banking sector dominates the financial sector of the country. Banking sector has experienced so many ups and downs during its journey after the independence. Several reforms initiatives have been taken for the improvement of the constraints.

Although excessive government intervention, political involvement, corruption, operational efficiency at ownership and management level create obstruction in smooth functioning of banking, it is still contributing substantially in financial services, investment opportunities and above all in country's GDP growth.

Banking sector in Bangladesh started its journey in 1972 as country reconstruction tool after the liberation war of 1971. The sector then comprised the government sector banks established vide presidential order by means of acquisition of the banks performing in the East Pakistan (later Bangladesh). Ten years after the nationalization of banking sector, government started reform of banking sector and left few banks to private sector for better banking functions to ensure rapid industrialization, economic growth and overall development of the economy. Later in 1999 and in 2009, government permitted few other banks to strengthen banking sector performance, entrepreneurship development, industrialization and foster economic growth by means of more investment in prospective sectors.

Current status of banking industry: In 2017 banking sector was quiet resilient in Bangladesh. Total size of the assets in banking sector rose by 12.4 percent, deposits increased by 11.7 percent and Loans grew by 18.9 percent. In consideration of net NPL ratio, quality of asset slightly improved to 2.2 percent but gross NPL remained at 9.3 percent. ROA remained unchanged at 0.7 percent while ROE increased by .7 percent compared to the same of the previous year. Banking sector was compliant in reserve requirements-CRR and SLR, and Basel III liquidity -LCR and NSFR. Islamic banks showed a notable growth in balance sheet size and performed better than the conventional banks. New banks except one performed better than the industry average as well. Importantly, 88.6 percent of depositors of the banking sector were protected under the deposit insurance system.

Financial System of Bangladesh

Financial system is comprised of banks, insurance companies, and capital market. Bangladesh Bank (BB) [20] oversees activities of scheduled banks comprising specialized banks, state-owned banks, foreign commercial banks (FCBs), private commercial banks, and financial institutions (Table 3).

Table 3: List of the financial institutions in Bangladesh.

Sectors	Financial Markets	Institutions	Regulators
Formal Sector	**Money Market**	**Scheduled Banks (57)**	**Bangladesh**
		01. SCBs (6)	Bank
		02. PCB (40)	
		03. FCBs (9)	
		04. SDBs (2)	
		Financial Institutions (34):	
		01. Govt. Owned (2)	
		02. Others (32)	
	Capital Market	Stock Exchanges (02)	BSEC
		Merchant Banks (57)	
		Credit Rating Companies (9)	
	Insurance Market	Insurance Companies (78):	IDRA
		01. Govt. Owned (2)	
		02. Others (76)	

Market size and Market Growth Rate

The market size of banking sector can be determined based on transaction volume, number of customers, size of balance sheet, amount of loans and advances, collection of deposits, revenue earned, number of employees, networking in the form of branch dispersion, coverage of operational activities etc. The prospect of economic growth of Bangladesh in the near future solely depends on the economic reforms. Besides, a huge investment is required to ensure steady economic growth (Table 4).

Banking Sector Performance

As shown in (Table 5), SCBs holding of total assets in 2016 and 2015 were 27.60 percent and 27.53 percent respectively PCBs' share of total assets stood 65.02 percent in

Table 4: Structure of Banking system (June 2017) (Billion BDT).

Bank type	Number of banks	Number of branches	Total assets	Share of industry Assets	Deposits	Share of deposits
SCBs	6	3713	3339.79	26.99	2654.14	28.31
DFIs	2	1407	313.49	2.53	263.58	2.81
PCBs	40	4529	8136.32	65.76	6080.05	64.85
FCBs	9	71	582.33	4.72	377.60.71	4.03
Total	57	9720	12371.94	100	9375.38	100

Source: Bangladesh Bank (2017)

Table 5: Banking sector performance (In Billion Taka).

2015						2016				
Types of Bank	**No. of banks**	**Total assets**	**Share of industry assets**	**Deposits**	**Share of deposits**	**No. of banks**	**Total assets**	**Share of industry assets**	**Deposits**	**Share of deposits**
SCBS	6	2839.6	27.5	2254.8	28.44	6	3209.5	27.6	2535.4	28.4
DFIS	2	291.4	2.8	226.6	2.86	2	299.5	2.6	249.4	2.8
PCBS	39	6652.9	64.5	5110.4	64.46	40	7560	65	5788	64.8
FCBS	9	530.8	5.2	336.8	4.25	9	557.6	4.8	361.1	4
Total	56	10314.7	100	7928.6	100	57	11626.6	100	8933.9	100

Source: Bangladesh Bank (2017

2016 from 64.50 percent in 2015. The FCBs held 4.80 percent share of the total assets decreased by 0.35 percentages from the previous year. The DFIs' share of the total assets was 2.58 percent in 2016 against 2.82 percent in 2015.

Regulation of the Banking Industry

Banks are regulated by Bangladesh Bank. It also formulates regulatory framework for all banks regarding all banking functions including board structure, Ownership pattern, capital management, classification of loans, provisioning requirement, risk management, core risk management, automation, reporting and compliance etc. All the banks need to comply the regulatory instructions circulated from Bangladesh Bank as general policy for operation of banking activities

Analysis & Findings

A 12.4 percent growth was observed in asset size of the banking sector in 2017 (as shown in Table 5) primarily due to increase in loans and advances. Deposit growth was lower in 2017 than the loan growth. Rise in growth of loan is replaced by a negative growth in investments in government and other securities.

Nonperforming loans in the banking sector: Nonperforming loans ratio was almost stable in 2017 than that of the previous years as shown in Table 6. But, SCBs and SDBs faced high NPL ratio in recent years which became an area of concern for the banking industry. (Table 6 and Table 7) shows that Gross nonperforming loan (NPL) increased from 9.2 percent in 2016 to 9.3 percent in 2017. Except FCBs and SDBs gross NPL ratios of all banks went up during the final quarter of December 2016 and end-December 2017. FCBs gross NPL ratio declined moderately by 2.6 percentages during this period. Apart from this, increasing NPL ratio of SCBs drive the overall NPL ratio in the industry. SCBs gross NPL ratio increased by 1.4 percent i.e. from 25.1 percent in 2016 to 26.5 percent in 2017. NPL ratio of PCBs rose from 2016 to 2017 by .3 percent (from 4.6 percent to 4.9 percent).

Table 6: Trends of NPL ratios by type of banks (Percent).

Bank type	2009	2010	2011	2012	2013	2014	2015	2016	2017
SCBs	21.4	15.7	11.3	23.9	19.8	22.2	21.5	25.1	26.5
DFIs	25.9	24.2	24.6	26.8	26.8	32.8	23.2	26.02	23.4
PCBs	3.9	3.2	2.9	4.6	4.5	4.9	4.9	4.6	4.9
FCBs	2.3	3	3	3.5	5.5	7.3	7.8	9.6	7
Banking sector Total NPL	9.2	7.3	6.1	10	8.9	10	8.8	9.23	9.3
Source: Bangladesh Bank (2017)									

Table 7: Trends of Amount of NPLs by types of banks.

Bank type	2009	2010	2011	2012	2013	2014	2015	2016	Jun-17
SCBs	117.5	107.6	91.7	215.2	166.1	227.6	272.8	310.3	345.8
DFIs	42.1	49.7	56.5	73.3	83.6	72.6	49.7	56.8	55.2
PCBs	61.7	64.3	72	130.4	143.1	184.3	253.3	230.6	317.3
FCBs	3.5	5.5	6.3	8.5	13	17.1	18.2	24.1	23.2
Banking sector Total NPL	**224.8**	**227.1**	**226.4**	**427.3**	**405.8**	**501.6**	**594.1**	**621.8**	**741.5**
Source: Bangladesh Bank (2017)									

Corporate Governance in Banks

In the recent years Bangladesh Bank has undertaken few initiatives regarding governance in banks of those measures, formation of executive, audit and Risk Management Committee at the Board level of the banks for transparency, accountability and enhanced disclosure requirements. Besides, roles and functions of banks board as well as management have been redefined by bringing amendments in related clauses of Banking Company Act 1991 (revised in 2013) vide circular no-11 issued from Banking Regulation & Policy Department on 27 October 2013.

The main objectives of corporate governance are:

1. Maintaining an effective system to help banks achieve objectives and goals
2. Supervising and awarding actions of the management
3. Alleviating the conflicts of interest between different stakeholders (Shareholders, management and Board

Regulation relating to corporate governance: To enhance governance in banks Bangladesh bank issued circular no-11 on 27 October 2013 from Banking Regulation & Policy Department that prescribed the organizational structure regarding the formation of Board in a banking company. Besides, to strengthen authority & responsibility of board of directors, to enhance the board structure and authoritative power of the board and to increase involvement of board in the strategy formulation and decision making process, Bangladesh bank has introduced board reporting and evaluation culture. All these regulatory frameworks have given the corporate governance culture a formal shape in banking sector of Bangladesh. In addition to that, Bangladesh Bank has provided with the guideline for formation of different sub committees under the board to strengthen and enhance the capacity and capability of banks board functions. The responsibilities of board and its committees have been designed is such a manner that ensures the accountability and transparency of board along with the responsibility in monitoring, supervision and policy formulation. According to the Bangladesh bank circular the nature, type and board size, structure and the responsibility of the board members are as follows:

Formation & Responsibilities of Board of Directors of a Bank Company:

- To ensure good governance, following are the instructions given by Bangladesh Bank regarding constitution of board of directors, their duties & responsibilities and other related activities

- Formation of Board of Directors
- Appointment of New directors
- Removal of Directors from office
- Appointment of Alternate Director
- Depositor Director
- Duties of the Board of Directors
- Responsibilities of the Chairman of the Board
- Formation of committees from the Board of Directors
- Meeting of Board, Audit Committee, Risk Management Committee, Executive committee
- Qualifications of the Members
- Roles and Responsibilities of the Executive Committee, Audit Committee, Risk Management committee

Asset Quality

Loans and advances comprise the major portion of asset composition of banks. Concentration of loans and advances exposes banks to increased vulnerability to credit risk. Gross NPLs to total loans and net NPLs to net total loans are the two vital indicators to portray asset quality in loan portfolio of banks.

(Table 6) portrays ratio of NPL to total loans of all banks. It shows a combined declining trend of NPLs up to 2011 (6.1 percent) which substantially increased to 10.0 percent in 2012 and again decreased in 2013 to 8.9 percent. The ratio again rose in 2014 (9.69 percent) and slightly declined in 2015 (8.79 percent). NPL increased to 9.23 percent in 2016 due to increase in total classified loans, non-paid outstanding and non- or delay payment of the interest charged on loans.

Poor appraisal, lack of supervision of the loans eventually created poor quality assets for SCBs. However, a positive trend is seen in recovery of SCBs because of reforms measures from government and regulators alongside the internal mechanism of the banks in recent years.

(Table 7) exhibits the NPLs of different types of banks in amount from 2009 to 2016. It also shows that total NPLs of banks increased from BDT 594.1 billion in 2015 to BDT 621.8 billion in 2016. Besides, in 2016 all bank types except PCBs faced increased NPL.

The result of the information shown in (Table 6,7,8 & 9) shows that between assets size and NPL of banks, there exists a positive relationship i.e. bank with bigger assets size tends to face more nonperforming loan (Table 7 & 8). Relationship between AD ratio and NPL shows negative movement i.e. banks with higher with higher Advance Deposit Ratio (ADR) faces lower NPL due to large exposure in loan portfolio comparing to NPL amount (Table 6, 8 & 9) except State Owned banks which show larger NPL despite a lower AD ratio.

Table 8: Structure of Banking system (June 2017) (Billion BDT).

Bank type	Total assets	Share of industry Assets	Deposits	Share of deposits
SCBs	3339.79	26.99	2654.14	28.31
DFIs	313.49	2.53	263.58	2.81
PCBs	8136.32	65.76	6080.05	64.85
FCBs	582.33	4.72	377.60.71	4.03
Total	**12371.94**	**100.0**	**9375.38**	**100.0**

Table 9: Bank Cluster-wise ADR at end-Jun 2017.

Bank wise	ADR (%)
SCBs	51.3
PCBs	83.6
FCBs	68.1
DFIs	79.5
Industry	74

As observed in the NPL trend from 2013 (in Table 7) just after the introduction of new Corporate Governance framework by BB (as mentioned in circular no-11 on 27 October 2013) it is seen that banks with large board size (with more members in board) faces lower NPL indicating an inverse relation between size of board and NPL. This implies that board has a possession or involvement in the credit administration process. Similarly Presence of independent directors in board has shown a negative movement of NPL in the period between 2013 and 2017 which means that more independent directors in board can reduce the amount of NPL. In addition, a negative relation and a positive impact can be derived from the NPL trend just before (up to 2013) and after (from 2013-2016), the constituting audit committee of the at board level of the banks. Such falling or improved NPL position indicates that Audit committee ensures accuracy, compliance, monitoring and control of activities performed at management level which help banks in reducing bad credit proposals for approval and thus improve the NPL situation. Finally a newly formed committee i.e. Risk management committee (introduced in 2013) and its regular meeting also helped banks lower NPL in the recent days.

This study found the relationship between governance framework, structure, mechanism with NPLs by establishing relationship of corporate governance practice in different dimensions in banks of different size, nature and board composition. The board composition with independent directors, holding of Audit and Risk management committee meeting regularly can affect the Non-performing loan situation. Besides, NPL varies with the size of assets, loans and deposit amount of the banks. In the end, it can be said that regardless of size of business, board composition and tenure of business, corporate governance has a positive impact in management and control of NPLs in the banking industry.

Conclusions & Policy Implications

Non-Performing loans have become a major burden for the banking sector of Bangladesh by a significant increase in NPLs over the last two or three decades. In recent times, this situation has deteriorated through increase of NPL in an alarming way. This rapid increase in NPL took place due to selection of faulty and improper borrower, error in documentation process, faulty or defective collateral, error or wrong estimation of collateral value and above all lack of proper monitoring, supervision and follows up from Board, management and operational level. Supervisory steps at board level along with cautious move in sanction and approve of credit proposal, preventing undue influence and prudent management of credit process can reduce the NPL of banking industry.

Presence of corporate governance practice in banks in the form of board size, board meeting, independent directors in board, audit committee and risk management committee etc. can reduce the amount of NPLs in banks. Besides the efficient use of resources (total assets) and allocation of resources (Loans) based on quality and performance can also play vital role in reducing NPLs and improving asset quality. Based on the quantitative observations excerpt from the trend data and the qualitative judgment made in this study based on the movement and change of quantitative data over the years following are the few policy implications that may help banks to improve its corporate governance practice and the NPL scenario:

- The results show that inclusion of more professional persons on the board as directors affects NPL implying that more participation in board creates the opportunity of brainstorming regarding the analysis, evaluation of any decisions. Thus banks should include as many directors as possible in consideration of the regulatory framework.
- Relationship between the independent directors in board and the scenario of NPL in banks is negative. This might be possible because independent directors

are outsiders and they do not have any benefit in the regular banking operations which refrain them to take excessive risk in bad, non-viable and sensitive projects and thus help bank reduce NPL by controlling bad investments. So, banks can include independent directors with expertise, professional experience and relevant academic background (at least to the proportion prescribed in BSEC rules) in board to strengthen monitoring and supervision for the board level so that management can be constrained from taking risky bad investment projects.

- Diversity of expertise in board remain a strong tool in management of NPL due to a strong argument, discussion or thorough analysis of issues to reach a consensus lead to a better output in case of loan and NPL management of banks.

- Banks with active audit committee face lower NPL as per the analysis results of the study. Holding of audit committee meetings of the board on a regular basis can ensure accuracy in reporting, regularity in compliance and discipline in internal control mechanism which by turn refrain bank management in making unproductive and manipulated proposals and decisions. Thus, banks should frequently hold the meeting at audit committee which will ensure both the compliance of corporate governance side by side improve the quality of banking operations.

- Risk management committee plays the vital role in bank by focusing the key risk areas of the bank through regular compliance and reporting from business units. It helps reduce irregularity, deficiencies and wrong practices and ensures effective risk management in the entire banking system.

- The above mentioned policy implications outlined in accordance with the findings of the study might help banking industry improve the NPL scenario by improving the corporate governance practice in all spheres of the banking systems.

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