

Rating Rationale

Jebil’s Finance Limited

Rating/Grading

Facility/Instrument	Amount (Rs. In Million)	Rating/Grading	Rating Action
Rights Share Issue	231.165	CARE-NP IPO Grade 4 [IPO Grade Four]	Assigned

The explanatory notes regarding the Rating/Grading symbols of CARE Ratings Nepal Limited (CRNL) are attached as Annexure 1

CRNL has assigned grading of ‘CARE-NP IPO Grade 4’ to the proposed Rights Share Issue of Jebil’s Finance Limited (JEFL). ‘CARE-NP IPO Grade 4’ indicates Below Average Fundamentals. CRNL assigns IPO grades on a scale of Grade 1 to Grade 5, with Grade 1 indicating strong fundamentals and Grade 5 indicating poor fundamentals. CRNL’s IPO grading is an opinion on the fundamentals of the issuer. The grade assigned to any individual issue represents a relative assessment of the ‘fundamentals’ of the issuer. JEFL proposes 40% rights share issue of 2.31165 Million number of equity shares of face value of Rs.100 each at par aggregating Rs. 231.165 million.

Detailed Rationale & Key Rating/Grading Drivers

The grading assigned to the rights share issue of Jebil’s Finance Limited (JEFL) is constrained by its volatile interest income and declining trend in net profit over the past 3 years and subdued financial performance during H1FY18(Provisional), high geographical and borrower concentration, high non-performing loans, albeit some improvement in Gross Non-Performing Loans ratio over the period, low level of CASA and high deposit concentration, exposure to regulatory risk related to finance industry and competition from other big finance companies and banks. The grading, however, derives strength from long track record of operation with experience board and management team, high Capital Adequacy Ratio, diversified product portfolio distribution in different sectors and growth in loans & advances and deposits over the period.

Ability of the company to continue its growth momentum without compromising on asset quality, maintaining the Capital Adequacy Ratio and ability to manage the impact of any regulatory changes by NRB would be the key sensitivities.

Detailed Description of the Key Rating/Grading Drivers

Key Rating/Grading Weakness

Volatile interest income and declining trend in net profit over the past 3 years and subdued financial performance during H1FY18

The interest income and total income of the JEFL was volatile during the last 3 years. The interest income decreased by 2.76% during FY16 (refers to 12-month period ending mid July 2016) over FY15 and the same increased by 10.94% to Rs.164 Million during FY17 over FY16. The volatility in the interest income was mainly due to fluctuation of average interest yield on loan and advances. The volatile interest income of JEFL also lead to volatile total income of JEFL which declined by 6.91% in FY16 over FY15 and the same was increased by 13.24% to Rs. 178 Million during FY17 over FY16.

The net profit of JEFL has shown a declining trend over the last 3 years. The same declined by 11.88% during FY16 to Rs.43 Million over FY15 with a further decline of 15.55% to Rs.36 Million during FY17. The subdued net profit during FY17 was mainly due to decline in non-operating income and increase in operating expenses. On back of subdued net profit, JEFL's Return on Total Assets (ROTA) has been declining over the period; it declined from 4.49% in FY15 to 3.48% in FY16 and further declined to 2.54% in FY17. However, the company's interest spread increased from 2.14% during FY16 to 2.94% during FY17 due to high increase in Interest income/Avg. Interest earning assets (i.e. 209 bps to 11.15% over FY16) as compared to Interest cost/Average Borrowed Funds (i.e. 128 bps to 8.21% over FY16). JEFL's Net Interest Margin (NIM) increased to 4.19% in FY17 from 3.20% in FY16 due to increase in net interest income was proportionately higher than the increase in average total assets.

During H1FY18, the total income increased by 37.34% as compared to H1FY17 due to increase in interest income on back of increase in loan portfolio and non-operating income. However, PAT of the company declined by 71.82% during H1FY18 as compared to H1FY17 due to increase in interest expenses (i.e. 84.42%) on back of higher cost of funds because of liquidity crunch happen in financial market of Nepal and increase in employee expenses (i.e.50.6%) due to increase in salary. Tightening liquidity in banking sector during the end of FY17 resulted in increased cost of funds for banking sector in Nepal.

High geographical concentration

Despite long track of operations, JEFL operations is concentrated in only one district out of total 77 districts of Nepal through its office located at New road, Kathmandu and has no branches. As per banking and financial statistics publish by Nepal Rastra Bank, 28 finance companies have total of 130 branches as on July 15, 2017.

High Borrower Concentration

The exposure to top 20 borrowers of JEFL was Rs.402 Million as on October 17, 2017 (Rs.375 Million and Rs.374 Million respectively for July 15, 2017 and July 15, 2016). The top 20 borrowers constituted 35.52% of total loan portfolio as on October 17, 2017 (33.31% as on July 15, 2017 and 39.39% as on July 15, 2016) leading to high borrower concentration.

High Non performing loans, however, improvement in Gross Non-Performing loans ratio over the period

JEFL's Gross Non Performing Loan (GNPL) to the total loans has shown improvement over the period; declining from 5.41% at the end of FY15 to 4.79% at the end of FY16 and further declining to 3.05% at the end of FY17. However, it increased and was high at 4.84% as on Jan 14, 2018, mainly due to classification of an agricultural loan of Rs. 19 million (i.e. 1.65% of total loan) into non-performing loan during H1FY18. The industry GNPL ratio for Class 'C' Financial institutions as on Oct 17, 2017 was 13.23% and July 15, 2017 was 13.37%.

Low level of CASA and high deposit concentration

CASA deposits of JEFL declined to 25.26% as on July 15, 2017 from 37.75% as on July 15, 2016 and further to a low level of 19.13% as on October 17, 2017 due to decline in the saving deposits over the period and substantial increase in the fixed deposits. JEFL's CASA deposits level was lower as compared to industry average of 36% as on July 15, 2017 and 35% as on October 17, 2017. Further, the declining trend of CASA over the period resulted in increase in the cost of fund leading to lower profitability and adversely impacting the competitive position of the bank. As on July 15, 2017, the concentration on top 20 deposits was high and increased to Rs 361 million i.e. 31.53% of total deposits from Rs. 298 million i.e.30.69% of total deposits as on July 15, 2016.

Competition from other bank and financial institution and exposure to regulatory risk related to finance companies

The grading is constrained by presence of large number of finance companies in the industry along with Commercial and Development banks conducting similar kind of businesses and lending at lower interest rate than finance companies due to their ability to raise lower cost funds. Further, the Banking and Finance industry in Nepal is exposed to changes in the various regulatory measures issued by NRB from time to time.

Key Rating/Grading Strengths

Long track of operation with experienced board and management team

JEFL has been providing its services for more than eight years (since 2009). It has six experienced members on its board led by Mr. Binod Kumar Manandhar (Chairman), B.B.A Graduate, has 4 years of experience as director of Siddhartha Finance Ltd. (from 2001 to 2004) and currently engaged in tours and travel business. The day to day operations of the company are headed by Mr. Laxmi Lal Nakarmi, (CEO of JEFL), M.B.A, has 5 years of experience as account officer of Dom Consultancy Pvt. Ltd, 10 years of experience in Nepal Finance Ltd. as head of various departments and Managing Director of JEFL from 2009 to 2014 and CEO of this company since July, 2014. He is assisted by a team of professionals across various functions.

High Capital Adequacy Ratio (CAR)

JEFL has maintained a CAR of 45.43% at the end of H1FY18 which is high in comparison to the minimum regulatory requirement of 11% for 'C' class financial institution. The industry CAR as on July 15, 2017 was 21.19% and as on October 17, 2017, it was 20%. The CAR increased from 28.95% as on July 15, 2016 to 30.04% as on July 15, 2017 mainly due to higher increase in the share capital in comparison to risk weighted assets because of issue of bonus shares and accretion of profits to reserve and surplus during FY17. Further, the CAR of the company has been increased substantially to 45.43% as on Jan 14, 2018 from 30.04% as on July 15, 2017 due to higher increase in share capital (100% right issue made in October 2017 Rs.251.71 million) as compared to increase in risk weighted assets. JEFL capitalization level was improved after right issue made in FY18 and would be further strengthened after the proposed rights issue. Monetary Policy 2015-16 issued by NRB provisioned National Level Finance Companies would have to

increase minimum paid-up capital from existing Rs. 200 Million to Rs. 800 Million. JEFL's paid-up capital as on Jan 14, 2018 was Rs 569.56 Million and after the proposed right shares issue it is expected to meet the minimum regulatory requirement.

Diversified product portfolio

JEFL's credit portfolio was diversified in different sectors which consist of personal loans (15%), housing loans (21%), business loans (5%), auto loans (2%), hire purchase loans (16%), deprived sector loans (4%) and other loans (37%) as on July 15, 2017.

Growth in loans & advances and deposits

Over the period JEFL has demonstrated growth in loans and advances. The total outstanding loans and advances grew by compounded annual growth rate (CAGR) of 17.74% over last 3 years ending July 15, 2017. The total loan portfolio of the company has grown by 18.67% to Rs. 1,126 million at the end of FY17 from Rs. 949 million at the end of FY16. During H1FY18, the total loan portfolio of the company further grown by 2.3% to Rs. 1,152 Million. The deposits were grown by CAGR of 15.81% over last 3 years ending July 15, 2017. It was grown by 17.59% to Rs. 1,143 million at the end of FY17 from Rs. 972 million at the end of FY16. However, during H1FY18, the deposits of the company were declined by 3.68% to Rs. 1,101 million.

About the Company

Jebil's Finance Limited (JEFL) is a National Level 'Class C' Finance Company, commenced its operation from October 28, 2009. JEFL is promoted by individual promoters from diverse background with maximum shareholding by major shareholder ~5.5%. Its corporate office is located at New Road, Kathmandu Nepal. The share capital of the company is distributed among promoters and public (including staff) in the ratio of 51:49. The share capital of the company is listed in Nepal Stock Exchange. As on July 15, 2017, JEFL has market share of 2.29% in terms of credit portfolio and 2.19% in terms of deposits of finance companies' industry. JEFL is operating through its office located at New road, Kathmandu and has no branches.

During FY17 (Audited), JEFL has earned PAT of Rs.36 million (as against Rs. 43 million in FY16) with total outstanding loan portfolio of Rs. 1,126 million (as against Rs.949 million as on

mid-July 2016). Further, during H1FY18 (UA), JEFL earned profit of Rs.3 Million (as against Rs.9 million during H1FY17).

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Annexure 1

CARE Ratings Nepal – IPO Grading Scale

CARE IPO grade	Definition
CARE-NP IPO Grade 1	Strong fundamentals
CARE-NP IPO Grade 2	Above average fundamentals
CARE-NP IPO Grade 3	Average fundamentals
CARE-NP IPO Grade 4	Below average fundamentals
CARE-NP IPO Grade 5	Poor fundamentals

Note:

Modifiers {"+" (plus)} can be used with the grading symbols 2, 3 and 4. The modifiers reflect the comparative standing within the category.