

**Rating Rationale
ICFC Finance Limited**

Rating

Facility/Instrument	Amount (Rs. In Million)	Rating/Grading	Rating Action
Subordinated Debenture “12% ICFC Finance Ltd. Debenture 2083”	200.00	CARE-NP BBB- [Triple B Minus]	Assigned

CARE Ratings Nepal Ltd. (CRNL) has assigned ‘CARE-NP BBB-’ rating to the proposed Subordinated Debenture “12% ICFC Finance Ltd. Debenture 2083” issue of ICFC Finance Limited (ICFC). The instruments with this rating are considered to have moderate degree of safety regarding timely servicing of financial obligations, in Nepal. Such instruments carry moderate credit risk.

Detailed Rationale & Key Rating Drivers

The rating assigned to ICFC derives strength from the long track record of operation with experienced board and management team, considerable growth in business over the period with large market share in FY19 (refers to 12 months’ period ended Mid July, 2019), moderate capital adequacy level and good asset quality. The ratings also factor in diversified sector wise credit portfolio distribution, low concentration over top 20 depositors, healthy financial performance however, volatile over the period and comfortable liquidity profile. The rating, however, is constrained by low level of current and saving account (CASA) which is declining over the period, geographical concentration of business, increase in concentration over top 20 borrowers. Further the rating is constrained by significant decrease in fair value of investment over cost price despite diversified investment portfolio, exposure to regulatory risks related to finance industry and competition from other finance companies and banks.

Ability of the company to continue its growth momentum without impacting the asset quality and maintaining capital adequacy and ability to manage the impact of any regulatory changes by Nepal Rastra Bank (NRB) would be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strength

Long track record of operation with experienced board and management team

ICFC is operating since July 17, 2004 and guided by experienced Board of Directors (BoD) which includes eminent bankers, retired NRB officials, and professionals with wide experience in the financial and economic sector. ICFC BoD is chaired by Mr. Ram Babu Pant, who is a retired Deputy Governor of NRB with work

experience of more than 19 years and former CEO of ICFC with work experience of 12 years. The top and senior management team is composed of experienced banker having long track record of banking experience. Management team is led by Mr. Sunil Pant, CEO, who has more than 25 years of banking experience and has been working with ICFC since 2004 in various managerial positions. He has been supported by other experienced management team.

Considerable growth in business over the period with large market share

ICFC's loan portfolio and deposit grew by compounded annual growth rate (CAGR) of 22.03% and 22.35% respectively over last 3 years ending July 16, 2019 on back of increase in number of branches and effective marketing strategy (finance industry loan portfolio and deposit grew by CAGR of 6.83% and 5.74% respectively over last 3 years ending July 16, 2019). ICFC's loan portfolio grew by 24.71% to Rs 8,713 Mn in FY19 from Rs. 6,987 Mn in FY18 and deposit grew by 23.14% to Rs 10,933 Mn in FY19 from Rs 8,879 Mn in FY18 (higher than the growth in the finance industry loan portfolio and deposit in FY19). ICFC has 12.68% and 14.39% market share in terms of loan portfolio and deposit base of finance industry in FY19 (based on monthly data published by NRB).

Moderate capital adequacy level

ICFC's overall Capital Adequacy Ratio (CAR) stood moderate at 11.84% as on July 16, 2019 (13.08% as on July 16, 2018) as against regulatory requirement of 11% (finance industry has 20.42% CAR, based on monthly data published by NRB). CAR decreased in FY19 as compared to FY18 due to substantial increase in risk weighted assets (mainly credit portfolio) as compared to increase in capital fund by accretion of profit to reserve and surplus. After issue of proposed subordinated bond (if fully subscribed) its supplementary capital will strengthen further.

Good asset quality, better than industry average

ICFC's Gross Non performing Loan % (GNPL) is low at 0.08% in FY19 although increased slightly from 0.02% in FY18 (industry average GNPL was 8.8% in FY19). GNPL decreased to 0.02% in FY18 from 0.75% in FY17 (1.49% in FY16) mainly due to recovery of non-performing loans and increase in size of loan portfolio. In FY19, the delinquencies of more than 30 days amounted to Rs.144 Mn, that accounts for 1.65% of total advances (0.48% in FY18).

Diversified sector wise credit portfolio distribution

ICFC has been disbursing loans to various Industry/ Sector with 24.26% of total advances towards finance, insurance and real estate sector followed by 15.14% towards wholesaler & retail sector and 8.07% towards hotel and restaurant during FY19. In FY19, ICFC lent 17.27% (17.01% in FY18) towards productive sector;

of gross loans and advances outstanding prior to 6 months. Productive sector advances consist of 9.25% towards tourism sector, 3.88% towards cottage and small industries and 3.87% towards agricultural sector.

Moderate concentration over top 20 depositors

Deposit from top 20 depositors was moderate at 15.58% of total deposit in FY19 which increased from 13.68% in FY18. Top 20 depositors mainly consist of institutional depositors.

Healthy financial performance however, volatile over the period

During FY19, ICFC's total income increased by 34.12% to Rs. 1,371 Mn due to increase in both interest income and non-interest income. Interest income increased by 31.42% to Rs. 1,272 Mn during FY19 mainly due to growth in advances. Other non-interest income increased by 82.32% to Rs 99 Mn during FY19 mainly due to increase in fees and commission income. Net interest income increased by 39.30% to Rs.361 Mn during FY19. Cost of deposit decreased marginally to 8.77% in FY19 from 8.79% in FY18 due to slight decrease in proportion of fixed deposits and yield on advances increased to 13.97% in FY19 from 13.36% in FY18. Net Interest Margin (NIM) improved to 2.92% in FY19 from 2.66% in FY18.

ICFC's operating expenses increased by 28.15% during FY19 mainly due to increase in employee related expenses and office administration expenses. On back of sharp increase in total income as compared to increase in interest expenses and other non-interest expenses, it has reported increase in PAT by 75.89% to Rs.140 Mn during FY19 from Rs 80 Mn during FY18. Return on Total Assets (ROTA) has increased to 1.14% in FY19 (0.82% in FY18) and return on net worth (RONW) increased to 15.32% in FY19 (11.23% in FY18).

Comfortable liquidity profile

ICFC's liquidity profile as on July 16, 2019 show positive cumulative mismatches due to well matched tenure of assets and liability. Further, it has maintained CRR of 4.12% and SLR of 11.76% and as on July 16, 2019 which is in compliance with NRB norms of 4% and 7% respectively.

Key Rating Weaknesses

Low level of CASA declining over the period

ICFC maintained CASA proportion of 28.66% in FY19, which is lower than finance industry average of 32% for same period (based on monthly statistics published by NRB of Mid July, 2019) which resulted into high cost of fund and pressure on profitability. Further, CASA witnessed declining trend over the period, although it has slightly improved in FY19. CASA declined to 28.09% in FY18 from 52.50% in FY17 (Industry avg. CASA was 32.71% in FY18 and 35.70% in FY17). CASA proportion was in declining trend due to growth rate in fixed deposit was higher than growth rate in saving deposit as a result of competition from Bank and

Financial Institutions (BFIs) and higher interest rates prevailing in the market due to tight liquidity faced by banking sector of Nepal.

Geographical concentration of business

ICFC is operating in 3 provinces (i.e. Province 3, 4 and 5) and 8 districts of Nepal through its 18 branches, 1 extension counter and 15 ATM terminals (based on data published by NRB, 23 finance companies have 205 branches as on Mid July, 2019). Despite having large number of branches as compared to peers in finance industries, 14 branches are located in province 3 and ~79% of business, in terms of loan portfolio is concentrated over province 3. During current year, it has opened one branch in province 3 and has plans to open three new branches in eastern part of Nepal.

Increased in concentration over top 20 borrowers

Lending to top 20 borrowers increased to 24.75% of total loans and advances in FY19 from 20.66% in FY18. Due to high concentration over top borrowers there may be significant impact on assets quality, if any big borrower defaults on loan.

Significant decrease in fair value of investment over cost price despite diversified investment portfolio

ICFC's fair value of investment is Rs 1,060 Mn at the end of FY19 (cost price is Rs 1,101 Mn) which was Rs 762 Mn at the end of FY18 (cost price is Rs 764 Mn). Fair value of investment is Rs 40 Mn lower than its cost price in FY19 due to decrease in market price of equity investments and investments in mutual fund on back of decline in stock market of Nepal. Loss from change in fair value of trading assets was Rs 19 Mn during FY19 (Rs 48 Mn during FY18). However, the company earned interest and dividend income from investment in Securities/Bonds amounting to Rs 37 Mn during FY19 (Rs 29 Mn during FY18).

Exposure to regulatory risks related to Finance industry

The Banking and Finance industry in Nepal is exposed to changes in the various regulatory measures issued by NRB from time to time. In past, finance companies faced pressure from NRB for capital increment to Rs. 800 Mn from Rs. 200 Mn. NRB via its Monetary Policy has reduced the Statutory Liquidity Ratio (SLR) to 7% from earlier 8%; increased the priority sector lending requirement to 5% from earlier 4%; reduced the overdraft including personal loan of revolving nature to Rs 5 Mn from 7.5 Mn. Also, margin lending nature loan limit increased to 40% of primary capital from earlier 25% and percentage of deposit allowed to be received from any one institutional depositor reduced to 15% (earlier 20%). Hence, the banking and finance industry in Nepal is exposed to changes in the various regulatory measures issued by NRB from time to time.

Competition from other Finance Companies and Banks

As on Mid July, 2019, there are 23 finance companies operating with total 205 branches all over Nepal and ICFC has 17 branches. Industry (Class 'C' Banks-Finance Companies) has achieved total interest income of

Rs. 9,734 Mn in FY19 with Rs. 3,281 Mn net interest income; ICFC’s share in interest income and net interest income is ~13% (Rs. 1,265 Mn) and 10.82% (Rs 355 Mn) for the same period. Despite being a leading finance company in the industry, it is challenging for ICFC to maintain current market share and expand its business, due to high competition among banks and finance companies, existence of large number of finance companies along with Commercial and Development bank operating similar kind of businesses with ability to lend at lower interest rate and offer wider banking services than finance companies.

About the Company

ICFC is a national level class “C” finance company incorporated on September 22, 2003 as Investment and Credit Finance Company Limited which was changed to ICFC Finance Ltd. on March 1, 2010. It is licensed by NRB on July 14, 2004 and commenced operation on July 17, 2004. It is one of the leading finance company in Nepal. In terms of technology, it is using PUMORI PLUS IV software which enables to provide real time services to consumer across all branches. It has total assets size of Rs 13,812 Mn at the end of FY19 which grew by 26.89% over FY18. It has Rs 882 Mn paid up capital as on Mid July 2019 distributed among promoter and public shareholders in the ratio of 51:49 and the shares are listed in Nepal Stock Exchange Ltd (Rs 1,341 Mn market capitalization as on September 24, 2019). Mr. Purshottam Poudyal (6.35%), Mr. Sushil Kumar Pant (3.70%) and Mr. Ram Babu Pant (3.20%) are major promoter shareholders of the company.

Analyst Contact Mrs. Apsara Upreti apsara.upreti@careratingsnepal.com Tel No.: +977-01-4445473	Group Head Mr. Bidhan Ojha bidhan.ojha@careratingsnepal.com Tel No.: +977-01-4445474	Relationship Contact Mr. Sajan Goyal sajan.goyal@careratingsnepal.com Tel No.: 9818832909/+977-01-4445472/3/4
--	--	---

Disclaimer CRNL’s ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CRNL has based its ratings on information obtained from sources believed by it to be accurate and reliable. CRNL does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CRNL have paid a credit rating fee, based on the amount and type of bank facilities/instruments.
--