

## Rating Rationale

### Himalayan Bank Limited

#### Rating

Facility/Instrument	Amount (Rs. In Million)	Rating <sup>1</sup>	Rating Action
Issuer Rating	NA	CARE-NP A (Is) [Single A (Issuer)]	Reaffirmed
Subordinated Bond “10% Himalayan Bank Limited Bond 2083”	2,569.10	CARE-NP A [Single A]	Reaffirmed

\* Issued debenture amounting to Rs. 3,000 million, subscribed for Rs.2,569.10 million

CARE Ratings Nepal Limited (CRNL) has reaffirmed the issuer rating of “CARE-NP A (Is) [Single A (Issuer)]” assigned to Himalayan Bank Limited (HBL). Issuers with this rating are considered to offer adequate degree of safety regarding timely servicing of financial obligations, in Nepal. Such issuers carry low credit risk.

CRNL has also reaffirmed rating of “CARE-NP A [Single A]” assigned to the Subordinated Bond “10% Himalayan Bank Limited Bond 2083” issued by HBL. The instruments with this rating are considered to have adequate degree of safety regarding timely servicing of financial obligations, in Nepal. Such instruments carry low credit risk.

#### Detailed Rationale & Key Rating Drivers

*The ratings assigned to HBL derives strength from the long track record of the bank backed by institutional promoters, experience of directors and management team, adequate capitalization level, diversified and geographical coverage through the branch network in Nepal. The ratings also factor in consistent growth in deposits and advances, considerable growth in total income and profitability, diversified loan portfolio with regulatory compliance, comfortable Current Account and Savings Account (CASA) ratio though declining over the period and comfortable liquidity profile.*

*The rating, is constrained on account of moderate asset quality; however, better than industry average (for Class ‘A’ Commercial Banks), concentration in corporate loan portfolio, moderate deposits concentration and increasing advances concentration on top 20 individual borrower accounts during FY19, however in declining trend in 9MFY20, intense competition and exposure to regulatory risk related to industry.*

*The ability of the bank to continue its growth in business while maintaining asset quality and capital adequacy and ability to manage the impact of any regulatory changes by Nepal Rastra Bank (NRB) would be the key rating sensitivities.*

<sup>1</sup> Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com)

***Impact of COVID-19***

The current situation of COVID-19 pandemic which has led to disruption on overall industry and travel restrictions is likely to impact quality of bank's advances portfolio as well. Considering, current situation, NRB in March 2020, reduced Cash Reserve Ratio (CRR) from 4% to 3% providing additional liquidity to the Banks and also has reduced Bank Rate from 6% to 5%. Further, it has relaxed its asset classification guidelines till Mid-July 2020 whereby defaults in payment of due amount or renewal of short-term limits since quarter ending Mid-April 2020 doesn't entail downgrade of such assets. However, NRB also has directed Banks to provide rebate of 2% in interest rate for a quarter which will have negative impact on the profitability of the Bank in Q4FY20 (refers to period mid-April to mid-July 2020). As a result, in CRNL's view the credit risk profile of bank is expected to deteriorate over the medium term. Liquidity profile, resource raising ability and exposure to vulnerable asset classes and operating profiles in terms of geographies and borrower types would be critical monitorable factors in the banking sector. CRNL will continue to assess on the impact on the key business and financial parameters of banking sector and shall take appropriate rating actions if needed.

**Detailed Description of the Key Rating Drivers****Key Rating Strength*****Long track record backed by institutional promoters***

Operating since February 1992, HBL is providing banking services for more than 27 years. HBL was promoted by 'Employees Provident Fund (EPF)' and other investment companies as a joint venture with Habib Bank Limited (Habib) of Pakistan. Habib, which was the first commercial bank to be established in Pakistan in 1947 and is the largest private sector bank in Pakistan, holds 20% of paid up capital of HBL, while EPF, which is the state owned retirement fund of Nepal, established in 1934, under Ministry of Finance with principal objectives of managing Provident Fund in Nepal holds 14% of paid up capital of HBL. EPF managed provident fund with total fund of Rs.3,237 Bn as on January 14, 2020.

***Experience of directors and management team***

HBL is a professionally managed bank under the overall guidance of the bank's Board of Directors (BoD) which includes eminent bankers, businesspersons, etc. with wide range experience in the financial services and other sectors. Mr. Tulsi Prasad Gautam is the chairman of the bank since February 2020 and has more than 27 years of experience in different ministries/commissions of Government of Nepal and more than 5 years of experience in Nepalese banking sector. The senior management team of the banks is highly experienced in their respective field of operations. The bank is led by Mr. Ashok SJB Rana who is the Chief Executive Officer (CEO)), has 24 years of experience in HBL at different positions. Mr. Ejaz Qadeer Gill (deputed from Habib) is the Senior General Manager of HBL. Mr. Gill has 28 years of experience in different national and international banks at different positions. The senior management members have more than 2 decades of banking experience.

***Adequate capitalisation level***

HBL had paid up capital of Rs.8,520 Mn at the end of FY19 which was increased to Rs.9,372 Mn during 9MFY20 (refers to period from mid-July to mid-April 2020) by issuing 10% bonus shares out of distributable profits up to FY19 (refers to mid-July 2019). The bank reported Capital Adequacy Ratio (CAR) of 12.60% and Core Equity Tier- I (CET-I) of 11.63% as on July 16, 2019 as against the minimum regulatory requirement of overall CAR of 11% and CET- I of 7%. However, CET-I of the bank declined to 10.68% during 9MFY20 and overall CAR improved to 13.42% due to debenture issue.

***Diversified and geographical coverage through branches***

HBL has diversified presence all over the country through its 64 branches, 3 extension counter and 128 ATM Terminals as on January 14, 2020. The branches are spread over all 7 Provinces and cover 30 districts (out of total 77 districts) of Nepal.

***Consistent growth in deposits and advances***

Over the last 3 to 4 years the bank has shown consistent growth in the loans & advances and deposits. Total deposits of HBL have reached to Rs.113,090 Mn in FY19 recording a three-year CAGR of 9% and reported growth of 13.38% over FY18. Further, deposits of HBL increased to Rs.122,240 Mn during 9MFY20 reporting a growth of 8.09% over FY19. Bank's share of total industry deposits improved marginally from 3.81% as on July 16, 2019 to 3.83% as on April 12, 2020. HBL also reported consistent growth in total advances which stood at Rs. 98,206 Mn in FY19 recording a three year CAGR of 12.43% and reported growth of 13.08% over FY19. Further, total loans and advances increased by 11.99% to Rs.110, 346 Mn during 9MFY20 12.36% over FY19. HBL holds 3.93% and 3.86% of the industry advances during FY19 & 9MFY20 respectively. Credit to Core Capital and Domestic Deposits (CCD) ratio remains at 76.08% at the end of 9MFY19, which is close to maximum allowable CCD ratio (i.e. 80%).

***Considerable growth in total income and improvement in profitability***

During FY19, the bank's total income increased by 17.84% to Rs.13,340 Mn majorly due to rise in both interest income by 19.54% on back of growth in advances, increased interest rates leading to improvement in yield on advances and increase in the non-interest income by 7.44%. On back of these, Net interest income had increased by 16.42% to Rs.5,031 Mn during FY19. The yield on advances increased by 54bps to 11.68% and the cost of deposits increased by 68bps to 6.26% mainly due to increased volume of term deposits and decline in volume of CASA deposits and higher interest rates in the industry. The Net Interest Margin (NIM) of the Bank improved to 4.03% in FY19 as compared to NIM of 3.85% in FY18.

On the operational efficiency front, operating expenses have shown a y-o-y increase of 19.23%, mainly due to increase in employee related expenses as a result of revision in salaries. HBL's impairment charge for loans and other losses was Rs. 134 Mn in FY19 as against Rs. 680 Mn during previous year. HBL reported increase in

PAT Y-o-Y by 47.36% to Rs.2,764 Mn over FY18. Return on Total Assets (RoTA) of the bank improved substantially to 2.22% during FY19.

During 9MFY20, bank's total income increased by 6.94% to Rs. 10,432 Mn on back of increase in interest income. The Net interest income of the Bank increased by 2.32% to Rs. 3,842 Mn during 9MFY20 vis-à-vis 9MFY19. PAT of the Bank increased by 15.04% to Rs.2,317 Mn during 9MFY20 over 9MFY19. During 9MFY20, HBL booked non-operating income of Rs. 313 Mn on account of the partial portion of the disputed amount received in Q2FY20.

#### ***Loan portfolio diversified across industries with regulatory compliance***

HBL has diversified portfolio across sectors with 26.08% of the loan portfolio towards non-food production related sectors followed by lending towards wholesaler & retailer sectors with 17.17% as on July 16, 2019. During 9MFY20, lending towards Non-food production related manufacturing stood at 25.40% and lending towards wholesaler & retailer sectors stood at 19.76%. HBL's advances towards the productive sector were 32.65% as on July 16, 2019 and 54.98% as on April 12, 2020. Bank lent 5.26% as on July 16, 2019 and 5.42% as on April 12, 2020 towards deprived sectors. All these lending (i.e. Productive sector, agriculture & energy sector (combined) and deprived sector) are within the NRB requirements.

#### ***Comfortable CASA ratio although declining over the period***

HBL maintained comfortable CASA proportion of 49.12% during FY18, which declined to 44.26% during FY19 and increased slightly to 45.08% during 9MFY20. CASA proportion of HBL is better than the industry average of 41.77% & 40.23% for FY19 & 9MFY20 respectively.

#### ***Comfortable liquidity profile***

Bank has comfortable liquidity profile with positive cumulative mismatches as of April 12, 2020 due to well matched tenure of assets and liabilities. Further, HBL maintained SLR and CRR at 18.48% and 6.51% respectively at the last reporting week 9MFY20. Net Liquidity was 26.25% as on July 16, 2019 and 24.40% as on April 12, 2020. Maintained SLR, CRR and Net Liquidity are within the norms of NRB.

#### **Key Rating Weaknesses**

##### ***Moderate asset quality***

Absolute amount of Gross Non Performing Loans (GNPL) of HBL reduced from Rs. 1,218 Mn at the end of FY18 to Rs.1,099 Mn as on July 16, 2019 resulting into GNPL ratio improving to 1.12% as on July 16, 2019 (industry average GNPLs for FY19 is 1.40%) as compared to 1.40% as on July 16, 2018. GNPL ratio marginally improved to 1.11% during 9MFY20 and was better than the industry average GNPL ratio of 1.72%. The current situation of COVID-19 pandemic which has led to disruption on overall industry and travel restrictions is likely

to impact quality of bank's advances portfolio as well. Ability of bank to manage its asset quality would be key rating sensitivity.

#### ***Concentration in corporate lending portfolio***

Over the period, HBL has concentrated towards corporate sector portfolio. HBL has continuously increasing its lending proportion towards corporate sectors. As on July 16, 2019, the corporate segment constituted 73.58% of the total advances, which further increased to 74.55% of the total advances as on April 12, 2020.

#### ***Moderate deposits concentration and increasing advances concentration during FY19, however in declining trend in 9MFY20***

Deposit concentration of the top 20 depositors has been moderate of 26.70% of total bank deposits during FY19 which decreased marginally to 25.51% of total bank deposits during 9MFY20. Top 20 individual borrower's accounts for 16.86% of total advances during FY18, which was increased to 21.21% of total advances during FY19 which however reduced to 20.00% of total advances during 9MFY20.

#### ***Intense competition***

Currently there are 27 Commercial Banks, including three major state owned banks, operating with total 4,218 branches all over Nepal (based on Monthly statistics published by NRB for Mid-April 2020). HBL had 64 branches along with head office as on same date. Industry (Class 'A' Commercial Banks) has achieved total interest income of Rs.304,264 Mn during FY19 with Rs.127,266 Mn net interest income; HBL's share on interest income is 3.82% and 3.96% share on net interest income for the same period which reduced to 3.77% in terms of interest income and slightly increased to 3.84% in terms of net interest income during 9MFY20. Competition in interest rates is the prominent challenge in the Nepalese banking sector.

#### ***Exposure to regulatory risk related to industry***

The banking industry in Nepal is exposed to changes in the various regulatory measures issued by NRB from time to time. After the extensive capital increment pressure from Rs.2 Bn to Rs.8 Bn for Class "A" Commercial Banks, NRB decreased weighted average interest rate spread to 4.5% from earlier 5% for the FY19 and again decreased to 4.4% for the FY20 and has also changed the calculation method of interest rate spread via Monetary Policy, thereby impacting the absolute profitability of the banks. Also, to relax the liquidity crisis, Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR) has been reduced to 4% (further reduced to 3% amid COVID-19) & 10% respectively from existing 6% & 12% respectively. Further, NRB through its notice dated April 28, 2020 has directed BFIs to provide rebate of 200bps in calculation of interest rate for quarter ending Mid July 2020 which is likely to have significant impact on bank's profit.

#### **About the Bank**

Himalayan Bank Limited (HBL) is "A" class licensed institutions from Nepal Rastra Bank (NRB), listed in Nepal Stock Exchange is one of leading bank in Nepal. It was incorporated in joint venture with Habib Bank

Limited of Pakistan and obtained license to operate "A" class commercial bank from NRB dated February 18, 1992. Total shareholding of the bank is divided between promoter group and general public in the ratio of 85:15. HBL has wholly owned subsidiary company namely HBL Capital Limited. The bank reported PAT of Rs.2,764 Mn on an asset size of Rs. 133,033 Mn as on July 16, 2019. Further, HBL reported PAT of Rs. 2,317 Mn as on 9MFY20 (UA).

<b>Analyst Contact</b> Ms. Shalini Sanghai <a href="mailto:shalini.sanghai@careratingsnepal.com">shalini.sanghai@careratingsnepal.com</a> Tel No.: +977-01-4445473	<b>Relationship Contact</b> Mr. Sajan Goyal <a href="mailto:sajan.goyal@careratingsnepal.com">sajan.goyal@careratingsnepal.com</a> Tel No.: 9818832909/+977-01-4445472/3/4
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