

Corporate Development Bank Limited

Rating

Facilities	Amount (Rs. in Million)	Rating ¹	Rating Action
Issuer Rating	NA	CARE-NP B+ (Is) [Single B Plus (Issuer)]	Reaffirmed

CARE Ratings Nepal Limited (CRNL) has reaffirmed issuer rating of 'CARE-NP B+ (Is)' [Single B Plus (Issuer)] assigned to Corporate Development Bank Limited (CDBL). Issuers with this rating are considered to offer high risk of default regarding timely servicing of financial obligations.

Detailed Rationale & Key Rating Drivers

The rating assigned to CDBL continues to be constrained by its weak asset quality marked by high Gross Non Performing Loan (GNPL) ratio, small scale of operations with modest market share and higher concentration over top 20 depositors and borrowers. The rating is also constrained by limited reach of business, intense competition and exposure to regulatory risk related to banking industry.

The rating, however, derives strength from experienced management team, considerable growth in loans and advances and adequate level of capitalization. The rating also derives strength from moderate CASA level and liquidity profile of the bank.

Going forward, the ability of the bank to maintain its growth momentum while improving asset quality and its ability to manage the impact of any regulatory changes will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Weak asset quality

CDBL's Gross Non Performing Loan (GNPL) ratio stood high at 4.65% at the end of FY22 (Unaudited, refers to the twelve-month period ended mid-July 2022), which improved slightly from 4.70% at the end of FY21. This continues to remain substantially higher than the industry average GNPL ratio of 1.36% and 1.30% at the end of FY22 and FY21, respectively. Challenges in recoveries amid lingering impact of COVID, exacerbated further by the ongoing liquidity stress in the economy impacting borrowers' repayment ability remains a key concern and the bank's ability to improve its asset quality without major slippages going forward will be a key monitorable aspect. CDBL's GNPL ratio remained high at 4.69% as on mid-October 2022.

Modest financial performance, albeit on an improving trend during FY22

During FY22, CDBL's total income increased by 82.64% to Rs. 117 Mn on account of increase in interest income by 107.36% to Rs. 107 Mn backed by increase in loans and advances in FY22. Its yield on advances increased to 13.30% during FY22 from 13.18% during FY21, and that of the cost of deposits increased to 8.02% during FY22 from 6.90% during FY21. This led to increase in net interest income by 113.68% during FY22 to Rs. 56 Mn from 26 Mn in FY21. The net interest margin of CDBL improved to 4.46% in FY22 from 2.76% in FY21. Interest expenses also increased to Rs. 51 Mn in FY22 from Rs. 26 Mn in FY21 on account of substantial increase of deposits from customers. Accordingly, interest spread rate declined to 4.20% in FY22 from 4.68% in FY21. During FY22, CDBL's non-interest income increased by 22.59% to Rs. 9 Mn.

Operating expenses increased by 10.56% during FY22 due to increase in number of employees and other administrative expenses. Its operating expenses/ average total assets decreased to 2.35% in FY22 as compared to 2.81% in FY21. Impairment charge for loans and other losses increased to Rs. 20 Mn during FY22 as against Rs. 4 Mn during FY21 mainly due to increase in NPL as compared to FY21. With increase in income, the company has reported increase in PAT to Rs. 5 Mn during

¹Complete definition of the ratings assigned are available at www.careratingsnepal.com and other CARE publications

FY22 compared to loss of Rs. 34 Mn during FY21. Return on Total Assets (ROTA) and return on net worth (RONW) stood low at 0.37% and 0.72% respectively in FY22.

Furthermore, its net profit improved to Rs. 9 Mn during Q1FY23 as compared to profit of Rs. 1 Mn in Q1FY22 mainly due to substantial improvement in net interest income coupled with steady operating expenses. Net Interest Margin (NIM) ratio improved to 0.99% in Q1FY23 from 0.67% in Q1FY22. The net interest income improved to Rs. 19 Mn during Q1FY23 as compared to Rs. 8 Mn in Q1FY22. Also, return on Total Assets (ROTA) improved although remained low at 0.45% in Q1FY23 compared to 0.10% in Q1FY22.

High concentration over top 20 depositors and top 20 borrowers

CDBL's deposit from top 20 depositors was high at 18.89% of total deposit in FY22 which decreased from 42.02% of total deposit in FY21. Due to high concentration over top depositors, the liquidity position might be impacted in case of withdrawal of big deposits in short span of time. Furthermore, the bank also has concentration of loans and advances towards few borrowers group. CDBL's lending to top 20 borrowers group stood at 30.75% of total loans and advances at the end of FY22 and the same decreased from 46.37% over previous balance sheet date. Higher concentration over top borrowers increases risk on its assets quality due to increase in impact of any big borrowers default on loan. Furthermore, lending to top 20 individual borrowers remains steady at around 16.94% of total loans and advances in FY22 compared to 16.21% in FY21.

Limited reach of business

CDBL is operating in only one province (Province 2) having presence in single district of Nepal (out of 7 provinces and 77 districts of Nepal) through its 4 branches. On account of limited geographical presence, the business is concentrated towards limited customer base along with less diversified portfolio which increases the risk of volatility of a single economic region.

Competition from other bank and financial institutions

Currently, there are 17 development banks operating with total 1,118 branches all over Nepal (based on monthly statistics published by NRB for Mid-July, 2022) out of that CDBL has 4 branches. Industry (Class 'B' Development banks) has achieved total interest income of Rs. 55,444 Mn in FY22 with Rs. 18,254 Mn net interest incomes; CDBL's share on interest income and net interest income is ~0.19% (Rs. 107 Mn) and 0.31% (Rs 57 Mn) respectively for the same period. It is challenging for CDBL to grow from current market share and expand its business, due to high competition among bank and finance companies, existence of large number of Development bank along with Commercial and finance companies conducting similar kind of businesses and they lend at lower interest rate as well as they offer wider banking services than development banks.

Exposure to regulatory risk related to industry

The Banking and Finance industry in Nepal is exposed to changes in the various regulatory measures issued by NRB from time to time. From FY22 end, NRB has changed to Credit to Deposit (CD) ratio mechanism from existing Credit to Core Capital plus Deposit (CCD) ratio measures. CD ratio needs to be maintained below 90% from mid-July 2022 from earlier provision of 85% for CCD. Furthermore, risk weights of certain loans including personal overdrafts, TR loans, hire purchase loans for personal purpose, margin lending, etc. has been increased to 150% from existing 100% via the mid-term review of monetary policy issued by NRB for FY22. These changes are likely to put downward pressure on capital adequacy ratios of the banks and limit their ability for significant credit expansion, at least over the near term. Furthermore, bank rate has been increased to 8.5% from 7% and repo rate increased to 7% from 5.5% in the monetary policy issued by NRB for FY23. Increased bank rates will likely put upward pressure on both lending and deposit interest rates of the bank over the near term.

Key Rating Strengths

Experienced board members and management team

CDBL commenced its operations on October 14, 2007. It is a professionally managed development bank under the overall guidance of the Board of Directors (BoD) which includes eminent bankers and professionals with wide experience in the financial sector. Mr. Jainuddin Ansari (chairman of CDBL) is also chairman of National Medical College and has overall experience of more than 4 decades in diversified industries. The bank is led by CEO, Trilok Dhoj Joshi who has more than 29 years of banking experience. He was also associated with commercial banks in various positions for significant period of his total experience. CEO has been supported by other experienced management team.

Adequate level of capitalization

Overall capital adequacy ratio (CAR) decreased to 59.10% during FY22 from 70.37% in FY21, yet remained higher than the industry average of 13.10% as on mid-July 2022. Tier I Capital stood at 57.82% as on mid-July 2022 as compared to 10.02% in FY21. The Tier I Capital and overall CAR remained above the regulatory requirement of 6% for Tier I capital and 10% for overall CAR. The decline was mainly on account of increase in loans and advances by 136.03% in FY22. Furthermore, the CAR improved to 63.63% in Q1FY23.

Considerable growth in loans & advances and deposits over the period; albeit low market share

CDBL has reported high growth in the loan portfolio and deposits over the period. Total loan portfolio grew by year-on-year growth rate of 136.03% to Rs 975 Mn in FY22 (whereas development bank loan portfolio grew by 16.03% in FY22). Similarly, CDBL's deposit grew by year-on-year growth rate of 77.46% to Rs. 786 Mn in FY22 (whereas development bank deposit grew by 14.28% in FY22). Furthermore, during Q1FY23, credit portfolio grew to Rs. 987 Mn and deposit grew to Rs. 1,074 Mn.

Moderate CASA deposit ratio and liquidity profile

CDBL maintained CASA proportion of 27.92% in FY22 (higher than finance industry average of 25.62% in FY22) which decreased from 40.70% in FY21 (higher than finance industry average of 34.50% in FY21). However, CASA proportion was in declining trend due to growth rate in fixed deposit being higher than growth rate in saving deposit as a result of competition between Bank and Financial Institutions (BFIs) on taking fixed deposit at higher interest rate because of liquidity problem faced by banking sector of Nepal. Fixed deposit/total deposits increased to 59.86% in FY22 from 56.55% in FY21 (Industry avg. fixed deposit/total deposit was 64.21% in FY22 and 54.60% in FY21). CDBL has comfortable liquidity profile with positive cumulative balances as of mid-July 2022. However, during mid-October 2022, the CASA proportion increased to 44.86% on account of significant increment in current deposits to Rs. 362 Mn compared to Rs. 17 Mn in FY22.

About the Company

Corporate Development Bank Limited (CDBL) is a regional level class "B" Development bank incorporated on August 07, 2007. It was licensed by Nepal Rastra Bank (NRB) on October 11, 2007 and commenced operation on October 14, 2007. At the end of FY22, it has Rs. 500 Mn paid up capital paid up capital which is distributed among promoters and public shareholders in the ratio of 70:30.

Contact us**Analyst Contact**

Ms. Sarina Khakurel

Contact No.: 977-01-4012628

Email: sarina.khakurel@careratingsnepal.com

Mr. Santosh Pudasaini

Contact No.: +977-01-4012629

Email: pudasaini.santosh@careratingsnepal.com

Relationship Contact

Mr. Achin Nirwani

Contact No.: +977 9818832909

Email: achin.nirwani@careratingsnepal.com

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