

Rating Rationale
NIC Asia Bank Limited

Rating

Instrument	Amount (Rs. In Million)	Rating	Rating Action
Subordinated Bond “11% NIC Asia Bank Bond 2082/83”	1830	CARE-NP A [Single A]	Assigned

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

CRNL has assigned rating of ‘CARE-NP A (Single A)’ to the proposed Subordinated Bond “11% NIC Asia Bank Bond 2082/83” of NIC Asia Bank Limited (NIC Asia). 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 rating assigned to NIC Asia derives strength from the long track of operations, experienced promoters and management team, adequate capitalization level, geographical diversification through branches, consistent growth in loans & advances and deposits, considerable growth in total income and net profit over the period, good assets quality with declining GNPL ratio, diversified loan portfolio with focus on retail and SME segments, improving CASA ratio, comfortable liquidity profile and declining deposits concentration & moderate advances concentration. The rating, however, is constrained by decreasing return on total assets (RoTA); albeit improved during 9MFY18, increasing operating expenses, intense competition and exposure to regulatory risk related to industry.

Ability of the company to continue its growth momentum without compromising on 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, experienced promoters and management team

NIC Asia Bank was established in the year 1998 and has two decades of market presence. The bank’s profile derives strength from its strong promoters who are well experienced in the Banking, Insurance, Manufacturing, Import and Export, Trade sectors etc. NIC Asia is

professionally managed bank under the overall guidance of the bank's Board of Directors (BoD) which includes eminent Businessmen/ Industrialists with wide experience in the financial services. Mr. Tulsi Ram Agrawal is the Chairman of the bank, who has been engaged in industry, import export, banking and business sector for more than 3 decades.

The top and senior management team is experienced in their respective field of operations. The bank is led by its present Acting CEO, Mr. Roshan Neupane. Mr. Neupane is a qualified Chartered Accountant and has been working at NIC Asia Bank Limited since March 2008 at various managerial positions in the Bank and is assisted by senior management team members with vast experience in their respective fields. All the management members have minimum 3 years to 24 years of banking experience.

Adequate capitalisation & capital adequacy

Tier I capital adequacy of the bank stood at 9.16% as on April 13, 2018 (As on July 15, 2017: 12.38%) and overall capital adequacy stood at 13.03% (As on July 15, 2017: 13.83%) as against the regulatory requirement of 8% and 11% respectively as per Basel III norms of NRB. The bank has an adequate capital adequacy ratio inspite of the strong growth over the years due to regular capital infusion. During FY17 (refers to 12 month period ending mid July 2017), the bank has raised the paid-up capital by Rs.1,339 Mn through bonus shares issue and Rs.873 Mn through right share issue. Further, to strengthen the CAR, Bank has raised Rs.3 Bn by issuing "9% NIC Asia Debenture 2081/82" during H1FY18 having 7 years' maturity period and is going to raise Rs. 1.83 Bn by issuing 11% NIC Asia Bank Bond 2082/83 having 7 years maturity period.

Geographical diversification through branches

The bank has been aggressive on branch expansion over the period. During FY17, the bank has added 53 branches. NIC Asia has further opened 105 branches during 9MFY18. NIC Asia Bank has good geographical spread in Nepal with all over the country through its 224 branches, 14 extension counters and 213 ATM Terminals as per latest available data (i.e. as on Mid-June, 2018). The branches are spreaded over all 7 Provinces and covers 58 districts (out of total 77 districts) of Nepal.

Consistent growth in loans & advances and deposits

Over the last 3 years, the bank has shown robust growth in the loans & advances and deposits. Total deposits grew by 25% to Rs.87 Bn during FY17 as compared to FY16 and further increased by 54.25% to Rs.134 Bn as on April 13, 2018, on back of 53 new branch additions

during FY17 and further new branches added during 9MFY18. High addition of branches over the last 2 years coupled with aggressive lending by the bank, led to total advances growth of 22% during FY17 to Rs.72 Bn. The same further grew substantially by 50.17% during 9MFY18 to Rs.109 Bn over July 15, 2017 against industry increase of 8.42%. Due to this rapid pace of growth, the loan book is relatively unseasoned and has to see the test of time. Further, the ability of the bank to maintain the asset quality is the key rating sensitivity.

Considerable growth in total income and net profit over the period

During FY17, the bank's total income grew by 57% to Rs.7,986 Mn on the back of rise in both interest income by 57% on back of growth in advances & yield on advances and increase in the non-interest income by 58% on back of increase in investment income. However, the net interest income reported a lower growth of 30% to Rs.2,542 Mn in comparison to the increase in the total income mainly due to higher cost of deposits leading to increase in interest expenses.

The yield on advances increased by 178 bps to 10.07% and the cost of deposits increased by 159 bps to 5.49% during FY17. Increase in the yield on advances compared to lower increase in cost of deposits resulted into marginal improvement in the Net Interest Margin (NIM) to 2.83% in FY17 as compared to NIM of 2.78% in FY16. Significant decline in NPLs during FY17 led to decline in provision for loan loss expenses by 19.25% as compared to previous year. As a result of this, the net profit increased by 38% Y-o-Y to Rs.1,473 Mn in FY17.

During 9MFY18, bank's total income grew by 86% to Rs.9934 Mn compared to Rs.5332 during 9MFY17. However, the net interest income shown a lower growth of 44% to Rs.2655 Mn. in comparison to the increase in the total income mainly due to higher cost of deposits leading to increase in interest expenses on deposits by 128%. PAT of the bank declined by 18.51% to Rs.928 Mn during 9MFY18 due to substantial increase in Provision for Possible Losses as the volume of advances has increased substantially by 62% than that of 9MFY17. However, Profit before provisions has increased by 21% to Rs.1759 Mn during 9MFY18 over 9MFY17.

Good asset quality and declining GNPLs

The asset quality of the bank remained good reflected by GNPL% of 0.36% & 0.22% as on July 15, 2017 & April 13, 2018 respectively. This is in comparison to the average GNPL% of 1.54% & 1.52% for commercial banks (A class) as on July 15, 2017 & April 13, 2018 respectively. There was significant decrease in absolute amount of Gross NPLs from Rs.262 Mn (0.36% NPL)

as on July 15, 2017 to Rs.239 Mn. The bank has strengthened the recovery department with improvement in the tracking mechanism for NPLs.

Diversified loan portfolio, concentration towards retail and SME portfolio

NIC Asia has a diversified loan portfolio which consists of various types of loan disbursed over the period for various Industries/Sectors with maximum lending of 25.74% towards wholesale & retail sector as on April 13, 2018. Bank has shifted its concentration towards retail and SME portfolio rather than corporate sectors with a view of risk management. As on July 15, 2017, the corporate segment comprised of ~19% of the advances which has declined to 14.88% as on April 13, 2018; Retail portion (Retail plus SME & Deprived sector) comprised ~81% of the advances as on July 15, 2017 which has increased to 85.12% as on April 13, 2018. and Small & medium enterprises (SME) comprised 31.12%.

Improving CASA ratio

CASA deposits proportion has increased from 32.47% as on July 15, 2017 to 40.61% as on January 14, 2018, which has further improved to 43.69% as on 9MFY18 (Industry avg. for April 13, 2018 was 43.66%). The Term deposit/ Total deposits has decreased from 45.85% as on July 15, 2017 to 41.14% as on April 13, 2018 (Industry avg. for April 13, 2018 was 43.59%).

Comfortable liquidity profile

Bank has comfortable liquidity profile with positive cumulative mismatches upto 270 days, as on April 13, 2018, due to well matched tenure of assets and liabilities. NIC Asia has maintained SLR of 21.69% as on July 15, 2017 and 20.28% as on April 13, 2018 against industry average of 23.34% & 21.50% respectively; average CRR of 11.37% & 6.73% at the last reporting week as of FY17 and 9MFY18 respectively; Net Liquidity maintained at 25.80% as on July 15, 2017 and 20.42% as on April 13, 2018 against industry average of 29.65% & 25.23% respectively. Maintained SLR, CRR and Net Liquidity are within the norms of NRB.

Declining deposits concentration and moderate advances concentration

Deposit concentration to top 20 depositors has declined during 9MFY18 to 23% of total bank deposit (i.e. Rs.134 Bn) from 28% of total bank deposits (i.e. Rs. 87 Bn) as on July 15, 2017 and 25% of total bank deposits (i.e. Rs. 120 Bn) as on January 14, 2018. Moderate concentration on advances as top 20 individual borrowers accounts for 6.63% and top 20 group borrowers accounts for 8.32% of total loan portfolio (i.e. Rs. 109 Bn) as on April 13, 2018.

Key Rating Weaknesses

Decreasing return on total assets (RoTA), however improvement during 9MFY18

The ROTA of the bank declined to 1.02% during 9MFY18 which was 1.64% for FY17 and 1.76% at 9MFY17; due to substantial increase in assets base and on the other hand, the PAT declined by 18.51% as stated above. However, RoTA has improved to 1.02% during 9MFY18 as compared to 0.82% during H1FY18.

Increasing operating expenses

On the operational efficiency front, during FY17, the operating expenses have shown a y-o-y growth of 50.44% on account of branch expansion (53 branches added during FY17), increase in the number of employees to 1,755 against 1,101 employees at the end of FY16 and high expenses towards business promotion activities. The operating expenses/ average total assets increased to 1.76% in FY17 as compared to 1.49% in FY16. With further expansion in the branches, the operating cost may take some time to stabilize.

Intense Competition

Currently there are 28 Commercial Banks operating with total 2805 branches all over Nepal (based on Monthly statistics published by NRB for Mid-May 2018). NIC Asia has 224 branch along with head office and 15 extension counters as on Mid-June, 2018. Industry (Class 'A' Commercial Banks) has achieved total interest income of Rs.169,453 Mn during 9MFY18 with Rs.67,640 Mn net interest income; NIC Asia's share on interest income is 5.37% (Rs.9,095 Mn) and 3.93% share on net interest income (Rs.2,655 Mn) for the same period. Currently bigger banks are providing advances at the fine interest rates of 10%-14% p.a. to its customers, however Base Rate of NIC Asia is 11.50% as of April 13, 2018. Due to emergent competition it is challenges to recruit and retain skilled manpower. Unhealthy competition on interest rates is the prominent challenge. New technology based services and its growing demand among customers is fresh challenges for Nepalese banking sector.

Exposure to regulatory risk related to industry

The banking sector is reeling under capital increment pressure. Nepal Rastra Bank has extensively increased capital requirement for banking sector, i.e. from Rs. 2 Bn to Rs. 8 Bn for Class "A" Commercial Banks, due to which banks are facing investable amount deficit to grant new loans and advances. It's the new challenges to banking sector for financial performance as compared to capital increment in terms of Deposit, Credit, Profitability growth and payout to shareholders. As weighted average interest rate Spread shouldn't be more than 5% since FY15

stated by NRB and together with growing competition it has been decreasing continuously over the period thereby impacting profitability. Further the banking industry in Nepal is exposed to changes in the various regulatory measures issued by NRB from time to time.

About the Company

NIC Asia Bank Limited (NIC Asia) is “A” Class Licensed Financial Institutions from Nepal Rastra Bank (NRB) and is one of the top 5 “A” Class (Commercial) banks of Nepal in terms of Deposits and loans and advances as on April 13, 2018. It was incorporated on July 21, 1998 as Nepal Industrial & Commercial Bank Ltd., later it was merged with Bank of Asia Nepal Ltd. as on June 30, 2013 and named NIC Asia Bank Limited. The 93.48% of the total shareholding of the Bank is held by individual general public and 6.52% by corporate entities as on July 15, 2017; among which 51% belongs to promoter group shares and 49% belongs to general public. NIC Asia is *ISO 9001:2008* certified for *Quality System on Commercial Banking Activities*. The market share of NIC Asia Bank in terms of deposit base is 5.89% as on Mid-April 2018 and for the loan portfolio the market share is 5.44% as on Mid-April 2018 of industry (Class ‘A’ Commercial Banks). The Bank has two wholly owned subsidiary companies operating in Nepal namely NIC Asia Capital Limited (undertake Merchant Banking activities) and NIC Asia Laghubitta Bittiya Sanstha Limited.

The bank has achieved PAT of Rs.1,473 Mn on an asset size of Rs.99,232 Mn as on July 15, 2017 (A) as against PAT of Rs.1,067 Mn on an asset size of Rs.80,425 Mn as on July 15, 2016. Further, NIC Asia earned PAT of Rs.928 Mn during 9MFY18(UA).

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Annexure I

CARE Ratings Nepal – Symbols for Debt Rating in Nepal

Symbols	Rating Definition
CARE-NP AAA	Instruments with this rating are considered to have the highest degree of safety regarding timely servicing of financial obligations, in Nepal. Such instruments carry lowest credit risk.
CARE-NP AA	Instruments with this rating are considered to have high degree of safety regarding timely servicing of financial obligations, in Nepal. Such instruments carry very low credit risk.
CARE-NP A	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.
CARE-NP BBB	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.
CARE-NP BB	Instruments with this rating are considered to have moderate risk of default regarding timely servicing of financial obligations, in Nepal.
CARE-NP B	Instruments with this rating are considered to have high risk of default regarding timely servicing of financial obligations, in Nepal.
CARE-NP C	Instruments with this rating are considered to have high risk of default regarding timely servicing of financial obligations, in Nepal.
CARE-NP D	Instruments with this rating are in default or are expected to be in default soon.

Note:

- i. Modifiers {"+" (plus) / "-"(minus)} can be used with the rating symbols for the categories CARE-NP AA to CARE-NP C. The modifiers reflect the comparative standing within the category.