

Rating Rationale

NIC Asia Bank Limited

Rating

Facility/Instrument	Amount (Rs. In Million)	Rating	Rating Action
Subordinated Debenture “10% NIC Asia Debenture 2085/86”	4,000	CARE-NP A [Single A]	Assigned
Subordinated Debenture “11% NIC Asia Debenture 2082/83”	1,830	CARE-NP A [Single A]	Reaffirmed
Issuer Rating	NA	CARE-NP A (Is) [Single A (Issuer)]	Reaffirmed

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

CRNL has assigned ‘CARE-NP A’ rating to the proposed Subordinated Debenture “10% NIC Asia Debenture 2085/86” issue of NIC Asia Bank Limited (NIC Asia). CRNL has also reaffirmed Issuer rating of “CARE-NP A (Is)” and the rating of “CARE-NP A” assigned to the Subordinated Debenture (11% NIC Asia Debenture 2082/83) of NIC Asia. 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 rating assigned to NIC Asia derives strength from the long track record of operations, experienced promoters and management team, adequate capitalization, geographical diversification through branches, diversified loan portfolio with concentration towards retail and SME segments and improving CASA ratio. The ratings also factor in consistent growth in loans & advances and deposits, considerable growth in total income over the period; however decline in net profit during FY18 (refers to the 12 month period ended mid-July 2018), improved overall financial performance & profitability during Q1FY19 (refers to the 3 month period ended mid-October 2018), comfortable liquidity profile and moderate although declining deposits concentration. The rating, however, is constrained on account of moderation in asset quality during Q1FY19, however over GNPL% is at low level, increasing operating expenses, intense competition and exposure to regulatory risk related to industry.

Ability of the bank 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 of operations, experienced promoters and management team

NIC Asia Bank was established in the year 1998 and has more than two decades of track record and an established market presence in Nepal. The bank's profile derives strength from its strong promoters who are well experienced in sectors like banking, insurance, manufacturing, import and export, trading etc. NIC Asia is a professionally managed bank under the overall guidance of the bank's Board of Directors (BoD) which includes eminent businessmen and industrialists with wide experience in the financial services. Mr. Tulsi Ram Agrawal is the Chairman of the bank, who has been engaged in industry, banking and business sector for more than 3 decades.

The senior management team is experienced in their respective field of operations and is headed by Mr. Roshan Kumar Neupane (Chief Executive Officer, CEO), who is a Chartered Accountant by qualification and has been working at NIC Asia Bank Limited since March 2008 at various managerial positions. The Bank also appointed Mr. Sudhir Nath Pandey as Deputy CEO w.e.f. December 03, 2018. All the senior management team members have minimum 3 years to 24 years of banking experience.

Adequate capitalisation

The bank has maintained adequate capitalization levels. The bank reported Capital Adequacy Ratio (CAR) of 12.24% as on July 16, 2018 with Tier I CAR of 8.66% as compared to CAR of 13.83% and Tier I CAR of 12.38% as on July 15, 2017 as against minimum regulatory requirement of 11% stipulated by NRB in compliance with Basel III norms. As on October 17, 2018, the bank reported CAR of 12.48%. During FY18, the bank has raised Rs.3.00 Bn and during Q1FY19 raised Rs.1.83 Bn by issuing subordinated debentures to maintain and strengthen the adequate Capital Adequacy Ratio under Basel III norms.

Diversified and high geographical coverage through branches

NIC Asia Bank has diversified presence all over the country through its 264 branches, 25 extension counters and 257 ATM Terminals as per latest available data (i.e. as on October 17, 2018). The branches are spread over all 7 Provinces and cover 61 districts (out of total 77 districts) of Nepal. The bank has been aggressive in branch expansion over the period. During FY18, the bank has added 112 branches to reach at 231 branches and further added 33 new branches during Q1FY19.

Consistent growth in Loans & Advances and Deposits

Over the last 3 years the bank has shown robust growth in the advances and Deposits. The total deposits increased substantially by 73% to Rs. 151 Bn during FY18 over FY17 against industry growth of 18% and further increased by 11% to Rs. 167 Bn during Q1FY18 over FY18 against industry increase of 6.28%, on back of leveraging the new branch additions during FY18 & Q1FY19. Addition of branches over the last 2 years coupled with high focus on lending by the bank; the total advances book of the bank increased substantially by 67% during FY18 to Rs. 120 Bn over FY17 and further increased by 16% to Rs. 139 Bn during Q1FY18 over FY18. NIC Asia holds ~7% of the industry deposits and ~6% of the industry advances as on October 17, 2018 as per the monthly statistics published by NRB for the Mid October 2018. Due to the rapid growth over the short period, the loan book is relatively unseasoned and the ability of the bank to maintain the asset quality is the key rating sensitivity.

Considerable growth in total income over the period, however net profit declined during FY18

During FY18, the bank's total income increased by 79% to Rs. 14,793 Mn majorly due to rise in interest income by 91% on back of high growth in advances and improvement in yield on advances and increase in the non-interest income by 8%. However, the net interest income shown a lower growth of 55% to Rs. 4,210 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.

The yield on advances increased by 306bps to 13.14% and the cost of deposits increased by 200bps to 7.17% mainly due to high volume of term deposits in the comparison of CASA deposits and higher interest rate during FY18 due to tight liquidity in the industry. Increase in the yields on advances compared to lower increase in cost of deposits resulted into marginal improvement in the Net Interest Margin (NIM) to 3.07% in FY18 as compared to NIM of 2.92% in FY17. Significant increase in loan and advances during FY18 leads to increase in provision for loan loss to Rs. 305 Mn as against Rs. 70 Mn reversal during previous year. On back of the above, the Net profit declined by 2.24% Y-o-Y to Rs. 1,335 Mn in FY18 with Return on Total Assets (RoTA) of 0.97% for FY18 (FY17 1.46%), though profit before provisions & income tax has been increased by 8% to 2,147 Mn during FY18 over FY17.

Increased overall financial performance and improved RoTA during Q1FY19

During Q1FY19, bank's total income increased by 90% to Rs. 5,357 Mn in comparison to Rs. 2,826 Mn during Q1FY18 on back of increase in interest income by 92% and increase in non-interest income by 70% over the same period. The Net interest income of the Bank increased by

212% to Rs. 1,863 Mn during Q1FY19 vis-a-vis Q1FY18 on back of substantial increase in interest income as compared to lower increase on interest expenses by 54%. PAT of the bank has increased by 170% to Rs. 753 Mn during Q1FY19 (Rs. 279 Mn during Q1FY18) and ROTA has been improved to 1.90% as on Q1FY19 which was 0.97% for FY18.

Diversified loan portfolio, concentration towards Retail and SME portfolio

NIC Asia's loan portfolio is diversified across sectors with higher lending of 25.09% towards wholesale & retail sectors followed by construction sector with 16.65% lending as on July 16, 2018. Bank has shifted its concentration towards retail and SME portfolio rather than corporate sectors with a view of risk management. As on July 16, 2018, the corporate segment comprised of 11.20% (18.62% as on July 15, 2017) of the advances and the loans towards retail and SME sector lending comprised of 79.70% of the total advances (improved from 75.55% as of July 15, 2017). Further, the concentration of advances was low with the top 20 individual borrowers was constituting 5.79% of total advances and the top 20 group borrowers accounted for 8.80% of total loan portfolio as on July 16, 2018.

Improving CASA Ratio

CASA deposits proportion of the bank has increased substantially from 32% as on July 15, 2017 to 39% as on July 16, 2018 (Industry avg. CASA for July 15, 2017 and July 16, 2018 was 43.11% & 42.93% respectively). CASA deposits in absolute amount increased by 111% to Rs. 59,301 Mn during FY18 as compared to FY17. Also the Term deposit/Total deposits declined from 45.85% as on July 15, 2017 to 43.33% as on July 16, 2018, which was same for the industry average of 43.33%.

Comfortable liquidity profile

Bank has comfortable liquidity profile with positive cumulative mismatches as on July 16, 2018, due to well matched tenure of assets and liabilities. Further, NIC Asia has maintained SLR of 21.21% as on July 16, 2018 and an average CRR of 10.64% at the last reporting week as of FY18; Net Liquidity of the bank was 24.75% as on July 16, 2018 against industry average of 27.89%. Maintained SLR (minimum 12%), CRR (minimum 6%) and Net Liquidity (minimum 20%) are within the norms of NRB.

Moderate although declining deposits concentration

Deposit concentration to top 20 depositors has been moderate and declined from ~28% of total bank deposits as on July 15, 2017 to ~22% of total bank deposits as on July 14, 2018.

Key Rating Weaknesses***Moderation in assets quality during Q1FY19, however, overall GNPL% is at low level***

There was significant increase in absolute amount of Gross NPLs from Rs. 84 Mn at the end of FY18 to Rs. 355 Mn as on Q1FY19 ended on October 17, 2018 with Gross NPL ratio of 0.26% (FY18: GNPL 0.07%). Although, GNPL% increased during Q1FY19, the same is at low level against average GNPL% of 1.50% for industry (Class 'A' Commercial Banks) during the same period. Provision coverage to Gross NPLs was 444.94% as on Q1FY19 (FY18: 1523%).

Increasing operating expenses

On the operational efficiency front, during FY18, the operating expenses have shown a y-o-y growth of 75% (P.Y 57%) on account of branch expansion, increase in the number of employees and high expenses towards business promotion activities. The Operating expenses/ average total assets increased to 2.42% in FY18 as compared to 2.03% in FY17. With further expansion in the branches and recruitment of new employees, the operating cost may take some time to stabilize.

Intense competition

Currently there are 28 Commercial Banks, including three major state owned banks, operating with total 3104 branches all over Nepal (based on Monthly statistics published by NRB for Mid-October 2018). NIC Asia had 264 branch and 25 extension counters as on October 17, 2018. Industry (Class 'A' Commercial Banks) has achieved total interest income of Rs. 244,379 Mn during FY18 with Rs. 102,550 Mn net interest income; NIC Asia's share in interest income was 5.54% and 4.10% share in net interest income for the same period. Due to emergent competition it is challenge to recruit and retain skilled manpower. Also high competition in interest rates is the prominent challenge faced by the 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 has now decreased weighted average interest rate spread to 4.5% from earlier 5% via Monetary Policy issued by NRB, for the FY19 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% & 10% respectively from existing 6% & 12% respectively. Further the banking industry in Nepal is exposed to changes in the various regulatory measures issued by NRB from time to time

About the Bank

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 Interest Income, Net Interest Income, Deposits and Advances as on October 17, 2018. It was incorporated as 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 93.68% of the total shareholding of the Bank is held by individual general public and 6.32% by corporate entities as on July 16, 2018; among which 51% belongs to promoter group shares and 49% belongs to general public. NIC Asia has certified by *ISO 9001:2008* Certificate for *Quality System on Commercial Banking Activities*. Bank has been awarded as Bank of the Year 2007 and Bank of the Year 2013 by The Financial Times, U.K.-The Banker. 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 (microfinance business).

The bank has achieved PAT of Rs.1,335 Mn on an asset size of Rs.170,893 Mn as on July 16, 2018 as against PAT of Rs.1,365 Mn on an asset size of Rs.103,073 Mn as on July 15, 2017. Further, NIC Asia earned PAT of Rs.753 Mn during Q1FY19 (UA).

Analyst Contact

Mr. Giri Raj Kandel
giriraj.kandel@careratingsnepal.com
Tel No.: +977-01-4232610

Relationship Contact

Mr. Sajan Goyal
sajan.goyal@careratingsnepal.com
Tel No.: 9818832909/+977-01-4233436

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Annexure 1

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.*