

Rating Rationale

NIC Asia Bank Limited

Rating

Facility/Instrument	Amount (Rs. In Million)	Rating	Rating Action
Subordinated Debenture “NIC ASIA Debenture 2083/84”	4,400.00	CARE-NP A [Single A]	Assigned
Subordinated Debenture “10% NIC ASIA Debenture 2085/86”	2,404.69*	CARE-NP A [Single A]	Reaffirmed
Subordinated Debenture “11% NIC ASIA Debenture 2082/83”	1,830.00	CARE-NP A [Single A]	Reaffirmed
Issuer Rating	NA	[CARE-NP] A (Is) [Single A (Issuer)]	Reaffirmed

* Issued debenture amounting to Rs. 4,000 million, subscribed for Rs. 2,404.69 million

CRNL has assigned ‘CARE-NP A’ rating to the new proposed Subordinated Debenture “NIC ASIA Debenture 2083/84” issue of NIC Asia Bank Limited (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, moderation in asset quality during 9MFY19, although overall GNPL% is at low level, geographical diversification through branches, diversified loan portfolio with focus on 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 9MFY19 (refers to the 9 month period ended mid-April 2019), comfortable liquidity profile and moderate although declining deposits concentration. The rating, however, is constrained on account of 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. All the senior management team members have minimum 3 years to 24 years of banking experience.

Adequate capitalisation

NIC Asia had paid up capital of Rs.8,031 Mn at the end of FY18. NIC Asia has issued and capitalized 10% bonus shares out of distributable profits up to FY18, during 9MFY19. Tier I capital adequacy ratio (CAR) of the bank stood at 8.66% as on July 16, 2018 and overall capital adequacy stood at 12.24% as against the regulatory requirement of 6.50% and 11% respectively stipulated by NRB in compliance with Basel III norms. As on April 14, 2019, NIC Asia reported Tier I CAR of 8.05% and overall CAR of 13.10%. During 9MFY19, the bank raised Rs.1.83 Bn and Rs.2.40 Bn by issuing subordinated debentures to maintain and strengthen the Capital Adequacy Ratio.

Moderation in assets quality during 9MFY19, although 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.671 Mn as on 9MFY19 ended on April 14, 2019 with Gross NPL ratio of 0.45% (FY18: GNPL 0.07%). Although, GNPL% increased during 9MFY19, the same is at low level against average GNPL% of 1.71% for industry (Class 'A' Commercial Banks) as on same date. Provision coverage to Gross NPLs was ~296% as on 9MFY19 (FY18: ~1523%).

Diversified and high geographical coverage through branches

NIC Asia Bank has a diversified presence all over the country through its 281 branches, 40 extension counters, 23 branchless banking and 289 ATM Terminals as on April 14, 2019. The branches are spread over all 7 Provinces and cover 62 districts (out of total 77 districts) of Nepal. The bank has been aggressive in branch expansion over the period. During FY18, bank added 112 branches and during 9MFY19 it has added 50 new branches.

Consistent growth in Deposits and Loans & Advances

Over the last 3 years the bank has shown robust growth in the Deposits and Loans & Advances. The total deposits increased substantially by ~73% to Rs.151 Bn during FY18 over FY17 against industry growth of ~18% and further increased by ~18% to Rs.178 Bn during 9MFY18 over FY18 against industry increase of ~10%, on back of leveraging the new branch additions during FY18 & 9MFY19. Addition of branches over the last 2 years coupled with high focus on lending by the bank; the total loans & advances increased substantially by ~67% during FY18 to Rs.120 Bn over FY17 and further increased by ~24% to Rs.149 Bn during 9MFY19 over FY18. NIC Asia holds ~7% of the industry deposits and ~6% of the industry advances as on April 14, 2019 as per the monthly statistics published by NRB for the Mid April 2019. 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 ~54% 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. 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 charge for loans and other losses 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 Rs.2,147 Mn during FY18 over FY17.

Increased overall financial performance & profitability during 9MFY19

During 9MFY19, bank's total income has increased by ~65% to Rs.16,340 Mn in comparison to Rs.9,931 Mn during 9MFY18 on back of increase in interest income by ~59% and increase in non-interest income by ~119% over the same period. The Net interest income of the Bank increased by ~101% to Rs.5,324 Mn during 9MFY19 vis-a-vis 9MFY18 on back of substantial increase in interest income as compared to lower increase on interest expenses by ~43%. PAT of the Bank has increased by ~145% to Rs.2,276 Mn during 9MFY19 and ROTA has been improved to 1.60% as on 9MFY19 which was 0.97% for FY18.

Diversified loan portfolio with focus on 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 focus 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 which were further reduced to 5.00% and 6.26% during 9MFY19 respectively.

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 upto 270 days, as on April 14, 2019, due to well matched tenure of assets and liabilities. However, the assets and liabilities show cumulative mismatches during 271 to 365 days and after that has cumulative positive mismatches. Further, NIC Asia has maintained SLR of 15.11% as on April 14, 2019 and an average CRR of 5.77% at the last reporting week as of 9MFY19. Net Liquidity of the bank was 25.99% as on April 14, 2019. SLR (minimum 10%), CRR (minimum 4%) and Net Liquidity (minimum 20%) maintained by the bank 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 during FY17 to ~22% of total bank deposits during FY18, which has further declined to ~17% of total bank deposits during 9MFY19.

Key Rating Weaknesses***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 3309 branches all over Nepal (based on Monthly statistics published by NRB for Mid-April 2019). NIC Asia had 281 branch, 40 extension counters and 23 branchless banking as on April 14, 2019. Industry (Class "A" Commercial Banks) has achieved total interest income of Rs.244379 Mn during FY18 with Rs.102550 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 April 14, 2019. 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*. 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).

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