

**Rating Rationale**

**Rastriya Banijya Bank Limited**

**Rating**

Facility/Instrument	Amount (Rs. In Million)	Rating <sup>1</sup>	Rating Action
Subordinated Debenture (RBBL Debenture 2083)	2,500.00	CARE-NP A+ [Single A Plus]	Assigned
Issuer Rating	NA	[CARE-NP] A+ (Is) [Single A Plus (Issuer)]	Assigned

CARE Ratings Nepal Limited (CRNL) has assigned the issuer rating of “CARE-NP A+ (Is)” to Rastriya Banijya Bank Limited (RBB). 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 assigned rating of ‘CARE-NP A+’ to the proposed Subordinated Debentures issue of RBB. 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 RBB derive strength from the long track record of operations, ownership by Government of Nepal (GoN) & experienced management team, adequate capitalization, diversified and geographical spread pan Nepal through network of branches, diversified loan portfolio with concentration towards retail and SME portfolio and strong Current Account Saving Account (CASA) ratio with lowest cost of funds in the banking industry in Nepal. The rating also factors in consistent growth in total income and net profit over the period, comfortable liquidity profile and moderate deposits concentration & low advances concentration. The rating, however, is constrained on account of weak asset quality leading to high Gross Non Performing Loan (GNPL) level, intense competition and exposure to regulatory risk related to industry. The ability of the bank to continue its growth momentum without impacting the asset quality, maintaining capital adequacy, ability to manage the impact of COVID-19 and any regulatory changes by Nepal Rastra Bank (NRB) along with continued majority shareholding and support by GoN would be the key rating sensitivities.

**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 the 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.

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

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, ownership and expected support by Government of Nepal and experienced management team***

RBB was established in 1966 as the second commercial bank of Nepal and over the years has strong presence in Nepal with 240 branches and 198 ATMs (as on Mid-April 2020) covering all provinces and districts of Nepal. RBB is promoted by Government of Nepal (GoN) with 99.97% of its shares held by different Ministries of GoN. Further, the bank is managed under the overall guidance of Board of Directors who are appointed by GoN.

Mr. Nirmal Hari Adhikari is the Chairman of the bank and is a former Joint Secretary for Ministry of Finance. The top and senior management team of the bank is highly experienced in their respective field of operation and is headed by Mr. Kiran Kumar Shrestha, Chief Executive Officer (CEO), who has vast experience in Banking sector. Mr. Shrestha is supported by other experienced team members.

#### ***Adequate capitalization***

RBB had paid up capital of Rs.9,005 Mn at the end of FY19 (refers to the 12 month period ended mid-July 2019). Core Equity Tier I (CET-I) ratio of the bank stood at 12.31% as on July 16, 2019 against minimum requirement of 7% and overall capital adequacy ratio stood at 13.39% (11.22% at the end of FY18) as against the regulatory requirement of 11%. Accretion of the profit to the reserves was the main reason for improvement of overall CAR during FY19. RBB maintained 12.08% CET-I and 13.27% overall CAR during 9MFY20 (Unaudited, refers to 9 month period ended mid-April 2020). Further, the proposed debenture issue will help the bank improve its overall CAR.

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

RBB Bank has a diversified presence all over the country through its 240 branches, 17 extension counters, 93 branchless banking and 198 ATM Terminals as April 12, 2020. The branches are spread over all 7 Provinces and covers all 77 districts (out of total 77 districts) of Nepal.

#### ***Diversified loan portfolio, concentration towards Retail and SME portfolio***

RBB has diversified loan portfolio distribution with higher lending of 31.50% in FY19 and 30.47% in 9MFY20 towards sectors like wholesalers & retailers with next major lending is towards consumption loans. RBB's advances portfolio is concentrated towards retail and SME portfolio. Retail portfolio, including Small & medium enterprises (SME), sector lending proportion constitutes 70.64% of the advances as on July 16, 2019 (73.32% as on July 16, 2018).

As on July 16, 2019 the corporate segment comprised of 21.86% (19.43% as on July 16, 2018) of the advances. RBB lent 28.66% as on July 16, 2019 and 29.63% as on January 14, 2020 towards priority sector; of gross loans and advances outstanding prior to 6 months. Out of priority sector advances RBB lent 13.49% as on July 16, 2019 & 14.02% as on April 12, 2020 towards Agriculture sector and 15.18% as on July 16, 2019 and 15.61% as on April 12, 2020 towards energy & tourism sector (combined). Bank adequately lends to deprived sector; 5.14% as on July 16, 2019 and 5.57% as on April 12, 2020. All these lending (i.e. priority sector, agriculture, energy & tourism sector (combined) and deprived sector) are within the NRB regulatory norms.

***Strong CASA ratio with lowest cost of funds in the industry***

RBB has strong CASA deposits in its total deposits mix compared to industry average leading to the lowest cost of funds among its peers. RBB reported high CASA deposits proportion of 80.03% at the end of FY19 which declined to 75.44% at the end of 9MFY20 although reporting better than industry average. (Industry avg. CASA for FY19 & 9MFY20 were 41.77% & 40.23% respectively). CASA deposits in absolute amount increased by 11.54% to Rs. 154 Bn during FY19 as compared to FY18 and however declined marginally by 0.79% during 9MFY20 over FY19. High CASA proportion has led to lowest cost of funds for RBB among other banks providing competitive advantage to RBB in base rate plus regime. RBB reported cost of funds of 3.53% during FY19 and 4.19% during 9MFY20.

***Considerable growth in total income and net profit over the period***

During FY19, bank's total income increased by 23.11% to Rs. 16,729 Mn majorly due to rise in both interest income by 23.35% on back of growth in advances, increased interest rates leading to improvement in yield on advances and increase in the non-interest income by 21.12%. However, interest expense also increased substantially during the period reporting an increase of 66.75% due to increase in deposit interest rates. On back of these, net interest income increased by 9.15% to Rs. 9,948 Mn during FY19 against Rs 9,114 Mn during FY18. The yield on advances increased by 30 bps to 9.88% and the cost of deposits increased by 89 bps to 2.73% during FY19 over FY18. However, Net Interest Margin declined during FY19 by 14 bps to 4.71% over FY18 due to higher increase in interest expenses and substantial increase in average total assets during the period.

On the operational efficiency front, the operating expenses have been increasing y-o-y. However, during FY19, the operating expenses increased by 3.80% to Rs.4,527 Mn as compared to Rs.4,361 Mn in FY18.

RBB's impairment charge for loans and other losses declined in FY19 to Rs.611 Mn as against Rs.1,293 Mn during previous year. RBB reported PAT of Rs.5,047 Mn in FY19 as compared to PAT of Rs.3,659 Mn reported in FY18. Return on Total Assets (RoTA) of the bank has improved to 2.39% during FY19 which was 1.95% during FY18.

During 9MFY20, bank's total income has increased by 14.73% to Rs.13,882 Mn on back of increase in interest income by 16.29%. However, net interest income of the bank declined by 5.52% to Rs.6,972 Mn

during 9MFY20 vis-a-vis 9MFY19 due to increase in interest expenses by 62.68% which was higher than increase in interest income.

Further, PAT of the Bank has declined by 13.23% to Rs.3,036 Mn during 9MFY20 (Rs. 3,499 Mn during 9MFY19) on back of decline in net interest income. ROTA of the bank has decline to 1.81% during 9MFY20.

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

RBB has maintained a strong liquidity position with SLR of 30.25% as on July 16, 2019 and 29.96% as on April 12, 2020 vis-à-vis regulatory requirement of 10%; CRR of 7.61% as on July 16, 2019 and 5.96% as on April 12, 2020 vis-à-vis regulatory requirement of 4% which has been reduced to 3% since March 29, 2020; Net Liquidity of 35.60% as on April 12, 2020 vis-à-vis regulatory requirement of 20%. Maintained SLR, CRR and Net Liquidity are within the regulatory norms of NRB. Bank has moderate liquidity profile with positive cumulative mismatches as on April 12, 2020 due to well matched tenure of assets and liabilities.

#### ***Moderate deposits concentration and low advances concentration***

Deposit concentration to top 20 depositors has been moderate at 22.03% of total bank deposits as on July 15, 2019, however the same has increased to 27.52% of total bank deposits as on April 12, 2020. The concentration on advances to top 20 individual borrowers was low at 7.82% during 9MFY20 respectively and top 20 group borrowers accounts for 7.95% during 9MFY20 respectively of total loan portfolio.

### **Key Rating Weaknesses**

#### ***Weak Asset quality with high GNPL Level***

RBB's asset quality is marked by high Gross Non-Performing Loan (GNPL) which is highest in the industry. Bank reported GNPL ratio of 4.75% during FY18 which increased marginally to 4.79% during FY19 and improved to 4.63% during 9MFY20. In absolute amount, Bank reported GNPL of Rs. 7,092 Mn at the end of FY19 which declined marginally to Rs. 7,053 Mn at the end of 9MFY20. Industry GNPL ratio was 1.40% at the end of FY19 and 1.72% at the end of 9MFY20. 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. Out of total advances, the delinquencies of more than 30 days accounted for 6.39% of total advances; the same has further increased by 108 bps at the end of 9MFY20 to 7.47% compared to FY19.

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

Currently there are 27 Commercial Banks, including two other major state owned banks apart from RBB, operating with total 4,218 branches all over Nepal (based on Monthly statistics published by NRB for Mid-April 2020). RBB had 240 branch 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; RBB's share on interest income is 4.90% and 7.82% share on net interest income for the same period. The market share of RBB was 5.13% and 6.96% in terms of interest income and net interest income

during 9MFY20 respectively. Competition in the 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**

Rastriya Banijya Bank Limited was incorporated by Government of Nepal (GoN) on January 23, 1966 as Rastriya Banijya Bank under the provisions of Rastriya Banijya Bank Act 1965. Later, pursuant to Companies Act 2063, the entity was converted to public limited company and was renamed as Rastriya Banijya Bank Limited (RBB). RBB is “A” Class Licensed Institutions from Nepal Rastriya Bank (NRB) and comes under the purview of Banks & Financial Institutions Act (BAFIA) with 99.97% share held by various ministries of Government of Nepal. The bank reported PAT of Rs. 5,047 Mn on an asset size of Rs. 226 Bn as on July 16, 2019. Further, RBB reported PAT of Rs. 3,066 Mn during 9MFY20. The Bank has one wholly owned subsidiary RBB Merchant Banking Limited which was incorporated in January 29, 2016 and is licensed by the Securities Board of Nepal (SEBON) to undertake Merchant Banking and Investment Banking services.

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