

Rating Rationale

Century Commercial Bank Limited

Rating

Facility/Instrument	Amount (Rs. In Million)	Rating ¹	Rating Action
Subordinated Debenture	2,200.00	CARE-NP BBB [Triple B]	Assigned
Issuer Rating	NA	[CARE-NP] BBB (Is) [Triple B (Issuer)]	Assigned

CARE Ratings Nepal Limited (CRNL) has assigned the issuer rating of “CARE-NP BBB (Is) [Triple B (Issuer)]” to Century Commercial Bank Limited (CCBL). Issuers with this rating are considered to offer moderate degree of safety regarding timely servicing of financial obligations, in Nepal. Such issuers carry moderate credit risk.

CRNL has also assigned rating of ‘CARE-NP BBB [Triple B]’ to the proposed Subordinated Debentures issue of CCBL. The 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.

Detailed Rationale & Key Rating Drivers

The ratings assigned to CCBL derive strength from the track record of operation, experience of directors and management team, comfortable capitalization, diversified and geographical coverage through branch network in Nepal and diversified loan portfolio. The ratings also factors in considerable growth in total income, however decline in net profit during FY19 (refers to the 12 months period ended Mid-July 2019) and moderate liquidity profile. The rating, however, is constrained on account of deterioration in asset quality with increase in slippages during FY19, high cost of funds as compared to the industry, low proportion of Current Account Savings Account (CASA) deposits, high portfolio concentration among top borrower groups and depositors, intense competition and exposure to regulatory risk related to Banking industry. The ability of the bank to grow its business while maintaining asset quality and capital adequacy and ability to manage the impact of COVID-19 and any regulatory changes by Nepal Rastra Bank (NRB) 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

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com

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 (refers to period ending Mid July 2020).

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

Track record of operation and experienced directors and management team

Established in the year 2010; CCBL has around one decade of operational history. CCBL is professionally managed bank under the overall guidance of Board of Directors (BoD). Mr. Rajesh Kumar Shrestha is the chairman of the Bank since March 2015. The top and senior management team is highly experienced in their respective field of operations. The bank is led by CEO, Mr. Tulasi Ram Gautam who has been CEO of CCBL since 2018. He has more than 35 years of banking experience. All the management members have wide banking experience.

Comfortable capitalization level

CCBL had paid up capital of Rs.8,415 Mn at the end of FY19. Core Equity Tier (CET-I) of the bank stood at 13.46% (against minimum requirement of 7%) as on July 16, 2019 which increased to 13.71% as on April 12, 2020. Similarly, overall capital adequacy stood at 14.27% as on July 16, 2019 which increased to 14.49% as on April 12, 2020. Overall CAR is expected to improve after issuance of proposed debenture.

Diversified and geographical coverage through branches

CCBL has diversified presence in Nepal with 113 branches, 10 extension counters, 16 branchless banking and 83 ATMs terminals as on April 12, 2020 across the country. The branches are spread over all 7 Provinces and cover 52 districts (out of total 77 districts) of Nepal.

Diversified loan portfolio

CCBL has diversified portfolio distribution with higher lending of 17.41% in FY19 and 17.06% in 9MFY20 (Unaudited, refers to 9month period ended Mid-April 2020) towards wholesalers & retailers sector Next major lending of 15.92% in FY19 and 15.87% in 9MFY20 is towards Non-food production related industries. CCBL lent 30.33% as on July 16, 2019 and 28.47% as on April 12, 2020 towards priority sector; of gross loans and advances outstanding prior to 6 months. Out of priority sector advances CCBL lent 10.17% as on July 16, 2019 towards Agriculture sector and 20.16% as on July 16, 2019 towards energy & tourism sector (combined). Bank adequately lends to deprived sector; 5.09% as on July 16, 2019. All these lending (i.e. priority sector, agriculture, energy & tourism sector (combined)) are within the NRB regulatory norms.

Considerable growth in total income however decline in net profit during FY19

During FY19, the bank's total income increased by 25.48% to Rs.8,497 Mn majorly due to rise in both interest income by 27.77% on back of growth in advances, increased interest rates leading to improvement in yield on advances and increase in the non-interest income by 1.85%. On back of these, net interest income increased by 35.05% to Rs.2,592 Mn during FY19. The yield on advances increased by 65 bps to 13.10% however cost of deposits increased by 15 bps to 8.28%. Net Interest Margin (NIM) of the bank increased from 3.13% in FY18 to 3.43% in FY19 due to increase in the interest income being more than increase in interest expenses.

On the operational efficiency front, operating expenses have been increasing y-o-y. In FY19, the operating expenses increased by 41.11% to Rs.1,629 Mn as compared to Rs.1,154 Mn in FY18. This is mainly due to 38.12% increase in other operating expenses and 31.15% increase in employee related expenses on back of supporting the branch expansion leading to increase in the number of employees. Increase in operating expenses led to increase in operating expenses/ average total assets to 2.16% in FY19 as compared to 1.88% in FY18 due to higher increase in operating expenses in contrast to growth in assets of the bank. CCBL's impairment charge for loans and other losses in FY19 increased substantially to Rs. 574 Mn from Rs. 38 Mn in FY18 due to decline in asset quality during FY19 with CCBL reporting NPL of 1.40% at the end of FY19 from 0.50% at the end of FY18. Due to increase in operating expenses and increase in impairment charges, CCBL reported decline in PAT in FY19. However, CCBL reported increase in profit before impairment charges with Rs. 1571 Mn during FY19 against Rs. 1362 during FY18. Return on Total Assets (RoTA) of the bank has declined to 0.90% during FY19 (FY18: 1.48%).

During 9MFY20, bank's total income has increased by 4.80% to Rs.6,622 Mn on back of increase in interest income by 5.27%. Net interest income of the bank increased by 14.19% to Rs.2,252 Mn during 9MFY20 due to increase in interest income. PAT of the bank has increased by 49.96% to Rs.916 Mn during 9MFY20 (Rs.611 Mn during 9MFY19) and Return on Total Assets (ROTA) improved to 1.54% during 9MFY20 which was 0.90% for FY19.

Moderate liquidity profile

CCBL has maintained SLR of 18.03% as on July 16, 2019 and 19.02% as on April 12, 2020 vis-à-vis regulatory requirement of 10%; average CRR of 7.89% and 3.03% at the last reporting week as of FY19 and Mid April 2020 vis-à-vis regulatory requirement of 4% which has been reduced to 3% since March 29, 2020; Net Liquidity of the bank was moderate at 23.79% as on July 16, 2019 and 22.07% as on April 12, 2020 vis-à-vis regulatory requirement of 20%. Maintained SLR, CRR and Net Liquidity are within the norms of NRB.

Key Rating Weaknesses***Deterioration in Asset Quality with increase in slippages during FY19***

Gross Non Performing Loans (GNPL) of the bank significantly deteriorated from 0.50% during FY18 to 1.40% during FY19 (industry average GNPLs for FY19 was 1.40%). Further, GNPL ratio deteriorated to

2.19% at the end of 9MFY20. In terms of absolute amount, GNPL increased from Rs. 275 Mn during FY18 to Rs. 839 Mn during FY19 and further increased to Rs. 1,314 Mn during 9MFY20. The delinquencies of more than 30 days accounts for 2.61% of total advances during FY19, which increased by 323 bps to 5.84% of total advances during 9MFY20.

Low CASA deposit ratio

CCBL maintained low CASA proportion of 29.22% during FY19, which is lower than its peers and industry average of 41.77% during the same period. CASA proportion of CCBL has slightly increased to 30.28% during 9MFY20. CASA deposits in absolute amount has increased over the period. CASA deposits have increased by 15.50% during FY19 over FY18, which further increased by 1.57% during 9MFY20 over FY19.

Higher cost of funds in the industry

The cost of funds of CCBL was high at 8.19% in FY19 which improved to 7.81% during 9MFY20. This is likely to be a competitive dis-advantage for the bank, especially in “base rate plus lending rate” regime. Reason for higher cost of funds is due to lower CASA ratio. Fixed deposit comprised 54.14% of CCBL’s total deposit mix in FY19 as compared to 46.31% in FY18, in contrary to CASA rising to 29.22% in FY19 from 27.02% in FY18. Fixed deposit of CCBL grew by ~25% in FY19 to Rs. 35,458 Mn over FY18 whereas CASA grew by ~16%.

High portfolio concentration among top borrower groups and depositors

Deposit concentration by top 20 institutional depositors has been high at 27.02% of the total bank deposits as on July 16, 2019, which increased marginally to 27.44% of the total bank deposits as on April 12, 2020. The bank has moderate concentration on single borrowers as top 20 single borrower accounts for 16.90% of total advances during FY19 which was slightly decreased to 16.33% of total advances during 9MFY20. However, the bank has moderately high concentration on group borrowers as top 20 group borrowers accounted for 22.52% of total advances during FY19 which slightly increased to 23.18% of total advances during 9MFY20.

Intense competition

Currently there are 27 Commercial Banks, including three major state owned banks, operating with total 4,218 branches all over Nepal (based on Monthly statistics published by NRB for Mid-April 2020). CCBL had 113 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; CCBL’s share on interest income is 2.59% (Rs.7,889 Mn) and 2.04% share on net interest income (Rs.2,592 Mn) for the same period. The market share of CCBL has reached to 2.52% and 2.25% 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

Century Commercial Bank Limited (CCBL) is "A" Class Licensed Institutions from Nepal Rastra Bank (NRB) which was incorporated on April 23, 2010 as Century Commercial Bank Ltd. Major promoter of CCBL is Asian Life Insurance Co. Ltd with shareholding of 2.22% as on Mid April 2020. The bank reported PAT of Rs. 676 Mn on an asset size of Rs. 78 Bn as on July 16, 2019. Further, CCBL reported PAT of Rs. 916 Mn during 9MFY20. CCBL acquired three 'B' Class Development Banks and two 'C' Class Finance Companies during FY17 and FY18. The bank has one subsidiary company, namely Century Capital Markets Ltd. (CCML), incorporated in FY16 and is licensed by the Securities Board of Nepal (SEBON) to undertake Merchant Banking activities in Nepal.

<p>Analyst Contact Mr. Bidhan Ojha bidhan.ojha@careratingsnepal.com Tel No.: +977-01-4445473</p>	<p>Relationship Contact Mr. Sajan Goyal sajan.goyal@careratingsnepal.com Tel No.: 9818832909/+977-01-4445472/3/4</p>
--	--

Disclaimer

CRNL's ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CRNL has based its ratings on information obtained from sources believed by it to be accurate and reliable. CRNL does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CRNL have paid a credit rating fee, based on the amount and type of bank facilities/instruments.