Rastriya Banijya Bank Limited

Rating

Facility/Instrument	Amount (Rs. in Million)	Ratings[1]	Rating Action
Issuer Rating	NA	CARE-NP A+ (Is) [A Plus (Issuer)]	Reaffirmed
Subordinated Debenture	2,500.00	CARE-NP A+ [A Plus]	Reaffirmed

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP A+ (Is)' assigned to Rastriya Banijya Bank Limited (RBB). Issuers with this rating are considered to have adequate degree of safety regarding timely servicing of financial obligations, in Nepal. Such issuers carry low credit risk.

CRNL has also reaffirmed the rating of 'CARE-NP A+' assigned to the Subordinated Debentures of RBB. 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 reaffirmation of ratings assigned to RBB continues to derive strength from its long track record of operations; ownership by Government of Nepal (GoN) along with experienced management team supported by diversified geographical coverage; adequate capitalization level; sustained growth in loans & advances and deposits, albeit some moderation in 9MFY22 (Unaudited, refers to the nine-month period ended mid-April 2022); comfortable liquidity profile; and diversified loan portfolio with regulatory compliance. The ratings also factor in strong deposit profile with low cost deposits, and moderate deposits and advances concentration.

The ratings, however, remain constrained by comparatively weak asset quality with relatively high Gross Non-Performing Loans (GNPL) ratio vis-à-vis industry average. The ratings also factor in muted financial performance marked by decline in revenue and profitability in FY21 (Audited, refers to the twelve-month period ended mid-July 2021), intense competition, and exposure to regulatory risk related to industry.

The bank's ability to maintain its asset quality will be critical for the bank's earning profile and profitability and would be a key rating sensitivity. Maintaining adequate cushion towards the capital adequacy requirements, and ability of the bank to manage the impact of any regulatory changes by NRB will also remain key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Long track record, ownership by Government of Nepal and experienced management team supported by diversified geographical coverage

Established in the year 1966 as the second commercial bank of Nepal, RBB has a well-diversified geographical reach in Nepal with 258 branches and 247 ATMs (as on Mid-January 2022) covering all seven provinces and all 77 districts. RBB is promoted by Government of Nepal (GoN) with 99.97% of its shares held by different Ministries of GoN. Furthermore, the bank is managed under the overall guidance of its Board of Directors who are appointed by GoN. Dr. Balram Pathak, Chairman, had earlier served as a BoD of Rastriya Beema Company and is currently a faculty of Economics at Tribhuvan University. The management team is led by Chief Executive Officer (CEO), Mr. Kiran Kumar Shrestha, who has over 35 years' experience in various financial institutions. He is supported by an experienced management team.

[1]Complete definitions of the ratings assigned are available at www.careratingsnepal.com and in other CRNL publications.

Adequate capitalization level

RBB's capitalization levels continue to remain adequate with reasonable cushion over the minimum regulatory requirements. The overall capital adequacy ratio (CAR) of the bank improved to 13.46% as on July 15, 2021 (as on July 15, 2020: 12.64%) boosted by increase in supplementary capital through issuance of debentures worth Rs. 2.5 Bn coupled with accretion of profits to the reserve, as against the regulatory requirement of 11% stipulated by Nepal Rastra Bank (NRB). Core Equity Tier I (CET-I) of the bank, however, moderated to 11.09% as on July 15, 2021 from 11.43% as on July 15, 2020 due to relatively higher credit growth during the year vis-à-vis core capital accretion. Furthermore, as on April 13, 2022, overall CAR improved to 13.49% and CET-I moderated further to 11.01%. The improved cushion in the capitalization levels would put the bank in a better position to absorb any losses, should they materialize, especially given the uncertainty surrounding credit recovery amid the lingering impact of the covid-19 pandemic. The bank's ability to maintain adequate cushion in the capital adequacy ratios will remain critical for its solvency and growth prospect.

Sustained growth in Loans & Advances and Deposits over the period, however moderation in 9MFY22

The bank's total loans & advances increased by 25.23% year on year (y-o-y) to Rs. 196,002 Mn at the end of FY21. The growth trend continued during 9MFY22, albeit at a slower rate, up 15.18% over FY21. Similarly, total deposits of the bank grew 15.27% y-o-y to Rs. 266,160 Mn in FY21; however, declined by 7.64% in 9MFY22 over FY21. The growth trend has moderated during 9MFY22 impacted by the liquidity issues in the country's economy amid lower remittance, increasing balance of payment deficit, and reduced government expenditure so far this year. Despite the moderation in 9MFY22, the overall banking industry along with RBB had recorded substantial growth in their loans & advances portfolio over FY20-FY21, despite the pandemic. Significant increase in loans & advances in a short span can put added stress to the asset quality, particularly amid the uncertainty regarding the residual impact of the pandemic on borrowers. However, in RBB's case, the growth in credit has been generally well supported by its growth in deposits as indicated by its comfortable Credit to Deposit (CD) ratio of 88.17% (below the regulatory requirement of less than 90% by mid-July 2022) compared to the industry average of 90.36% as on mid-April 2022.

Comfortable liquidity profile

RBB continues to maintain a comfortable liquidity profile with SLR of 32.54% and average CRR of 5.72% as on July 15, 2021. Although these ratios have moderated somewhat during 9MFY22 amid the declining liquidity in the industry with the bank's SLR declining to 20.77% and CRR to 4.58% as on April 13, 2022, these remain comfortably above the minimum regulatory requirement of 10% and 3%, respectively. Furthermore, net liquidity of the bank was 21.43% as on January 14, 2022 against the minimum regulatory requirement of 20%. Also, the bank had comfortable liquidity position in terms of asset-liability matching with positive cumulative mismatch as on April 13, 2022.

Diversified loan portfolio

RBB has a diversified loan portfolio with higher lending of 29.99% of total loans & advances as on April 13, 2022 towards consumption loans. Next major lending of 24.37% was towards wholesalers & retailers sector (wholesale trade of durables, non-durables, automotive dealer/franchise, other retail trade and so on). Furthermore, RBB lent 33.75% towards priority sector and 7.19% towards deprived sector as on April 13, 2022. RBB's lending to priority and deprived sector are above the NRB requirements. Diversified loan portfolio towards various sectors supports in maintaining better quality of advances during the time of stress in the sector or slowdown in the economy.

Strong deposit profile with low cost deposits

RBB continues to have a comparatively higher proportion of Current Account Saving Account (CASA) deposits to total deposits in the industry. RBB maintained around 75.41% CASA deposits at the end of FY21 which had increased from 74.19% at the end of FY20. However, CASA deposits declined marginally to 74.74% at the end of 9MFY22. CASA ratio continues to remain above industry average (industry avg. CASA ratio for FY21 and 9MFY22 were 43.94% and 38.62% respectively), which leads to lower cost of funds for RBB vis-à-vis peers and provides competitive advantage to RBB in the "base rate plus" lending rate regime.

Moderate deposits and advances concentration

Total deposits concentration by top 20 depositors was moderate at 23.59% of total bank deposits as on July 15, 2021 (July 15, 2020: 23.80), which increased slightly to 24.58% as on January 14, 2022. The concentration on advances to top 20 single borrowers was also moderate at 8.26% as on July 15, 2021, which decreased to 7.87% as on January 14, 2022. Top 20 group borrowers accounted for 9.62% of total loan portfolio as on July 15, 2021, which also decreased slightly to 9.20% of total loan portfolio as on January 14, 2022. Lower concentration towards advances and deposits normally decreases re-pricing risks at times of interest rate volatility.

Key Rating Weaknesses

Modest asset quality

RBB continues to have a weak asset quality marked by a relatively high GNPL level, although there has been substantial improvement over the past several years aided by improved recovery efficiency. The bank reported GNPL ratio of 3.07% at the end of FY21 which had improved from 4.08% at the end of FY20. The ratio remained stable at 3.07% at the end of 9MFY22. Restructured/refinanced loans due to the impact of covid-19 remained low at around 1.34% of total loans and advances at the end of FY21. Nonetheless, RBB's GNPL ratios are the highest in the industry with the industry average GNPL ratio of 1.41% at the end of FY21 and 1.32% at the end of 9MFY22.

Muted financial performance marked by decline in revenue and profitability

During FY21, bank's total income decreased by 2.33% yoy to Rs. 18,393 Mn majorly due to decline in interest income by 5.43% owing to lower interest rates. Cost of deposits decreased by 43 bps to 3.20% and the yield on advances decreased by 268 bps to 7.21%, impacted by decreased market interest rates on all type of deposits on back of excess liquidity in the market during FY21. Furthermore, Nepal Rastra Bank (NRB) reduced the interest spread to 4.4% from earlier 5% impacting the interest income of banks. Consequently, Net Interest Margin declined during FY21 by 99 bps to 2.85%. Although bank's total income increased to Rs. 15,511 Mn during 9MFY22 from Rs. 13,833 Mn during 9MFY21, profitability remained muted amid higher interest expense. Consequently, PAT decreased by 20.01% y-o-y to Rs. 2,617 Mn during 9MFY22. The ability of the bank to manage sustained growth in business while improving its asset quality will remain critical from credit perspective.

Intense competition

Currently there are 27 Commercial Banks, including three major state-owned banks, operating with total 4,949 branches all over Nepal (based on monthly statistics published by NRB for mid-April 2022). RBB had 257 branches along with head office as on same date. Industry (Class 'A' Commercial Banks) had achieved total interest income of Rs. 309,982 Mn during 9MFY22 with Rs. 109,123 Mn net interest income, where RBB's share on interest income was 4.52% (FY21: 4.97%) and on net interest income was 5.79% (FY21: 6.23%) for the same period. Intense competition in the banking industry results in a highly dynamic market with volatile market shares. Competition in the interest rates remains a prominent challenge.

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. NRB has changed to CD ratio mechanism from existing Credit to Core Capital plus Deposit (CCD) ratio measures. CD ratio needs to be maintained below 90% by mid-July 2022 from earlier provision of 85% for CCD. Furthermore, risk weights of certain loans including personal overdrafts, TR loans, hire purchase loans for personal purpose, margin lending, etc has been increased to 150% from existing 100% via the mid-term review of monetary policy issued by NRB for FY22. These changes are likely to put downward pressure on capital adequacy ratios of the banks and limit their ability for significant credit expansion, at least over the near term. Furthermore, bank rate has been increased to 7% from 5% and repo rate increased to 5.5% from 3.5% in the midterm review of monetary policy issued by NRB for FY22. Increased bank rates will likely put upward pressure on both lending and deposit interest rates of the bank over the near term.

About the Bank

RBB is an "A" Class Licensed Institution from Nepal Rastra Bank (NRB). It was incorporated on January 23, 1966. The bank has one subsidiary company operating within the territory of Nepal, namely RBB Merchant Banking Limited. As on Mid-January 2022, 99.97% of its shares are held by different Ministries of GoN, among which 93.33% is held by Ministry of Finance.

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