

NIC Asia Bank Limited (Revised)

Ratings

Facility/Instrument	Amount (Rs. in Million)	Ratings ¹	Rating Action
Issuer Rating	NA	CARE-NP A- (Is) [Single A Minus (Issuer)]	Revised from CARE-NP A (Is)
Subordinated Debenture (NIC ASIA Debenture 2083/84)	1,944.00	CARE-NP A- [Single A Minus]	Revised from CARE-NP A
Subordinated Debenture (10% NIC ASIA Debenture 2085/86)	2,404.69	CARE-NP A- [Single A Minus]	Revised from CARE-NP A
Subordinated Debenture (11% NIC ASIA Debenture 2082/83)	1,830.00	CARE-NP A- [Single A Minus]	Revised from CARE-NP A

CARE Ratings Nepal Limited (CRNL) has revised the issuer rating of NIC Asia Bank Limited (NIC Asia) to “CARE-NP A- (Is) [Single A Minus (Issuer)]” from “CARE-NP A (Is) [Single A (Issuer)]”. 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 revised the rating assigned to the Subordinated Debentures issued by NIC Asia to “CARE-NP A- [Single A Minus]” from to “CARE-NP A [Single A]”. 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 revision in the ratings assigned to NIC Asia takes into account the moderation in the capitalization levels of the bank following a high growth phase resulting in decreased cushion in its capital adequacy ratios, particularly tier 1 capital, at the end of FY21 (FY refers to the twelve-month period ended mid-July). The rating derives strength from the bank’s long track record of operations, experienced promoters and management team, diversified and high geographical coverage through branches, good asset quality, diversified loan portfolio with concentration towards retail and small & medium enterprise (SME) portfolio and healthy Current Account Savings Account (CASA) ratio despite some moderation during FY21-H1FY22 (H1FY22 refers to the six-month period ended mid-January 2022). The rating also factors in consistent growth in deposits and loans & advances and sustained growth in total income and net profits over FY21 and H1FY22. The rating, however, is constrained on account of moderate, albeit improving, capitalization levels during H1FY22 and moderate liquidity profile of the bank. The rating also factors in the intense competition and exposure to regulatory risk related to the banking industry in Nepal.

Going forward, the ability of the bank to sustain its growth in business while maintaining the profitability levels and without compromising on asset quality, improve capital adequacy indicators with adequate cushion to the minimum regulatory requirement levels 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 Strengths

Long track record of operation, diversified geographical coverage with experienced promoters and management team

Established in the year 1998, NIC Asia Bank has a strong presence in Nepal with 358 branches, 70 extension counters, 81 branchless banking and 472 ATMs as on January 14, 2022 covering all the Provinces in Nepal. The bank’s profile derives strength from its strong promoters who are well experienced in the banking, insurance, manufacturing, import and export,

trade sectors, etc. NIC Asia is managed bank under the overall guidance of the bank's board of directors which includes eminent Businessmen/Industrialists with wide experience in the financial services. Mr. Tulsi Ram Agrawal is the Chairman of the bank, who has experience of more than three decades in import export, banking and business sectors. The senior management team is experienced in their respective field of operations and is headed by chief executive officer Mr. Roshan Kumar Neupane, who is a Chartered Accountant by qualification and has been working at NIC Asia Bank Limited since March 2008 at various managerial positions. He is aptly supported by an experienced management team.

Good Asset quality

NIC Asia had Gross Non-Performing Loan (GNPL) ratio of 0.50% during FY21, which declined from 0.75% during FY20. GNPL has declined further during H1FY22 to 0.47%. GNPL in absolute numbers was Rs. 1,273 Mn at the end of H1FY22 compared to Rs. 1,317 Mn at the end of FY21. The improvement in GNPL levels during FY21-H1FY22 was aided by the relaxations provided by NRB amid the covid pandemic coupled with the higher base effect – due to the increased loans & advances during this period. Furthermore, the bank's covid19 related restructured/rescheduled portfolio remains under check and was below 1% of total loans & advances as on mid-January 2022. NIC Asia's GNPL ratio continues to remain well below that of the industry – industry GNPL ratio for FY21 and H1FY22 were 1.41% and 1.18%, respectively. Going forward, the ability of the bank to maintain its asset quality, especially in view of the lingering impact of the pandemic, remains critical for the bank's earning profile and profitability and will be a key rating sensitivity.

Increasing scale of operations backed by consistent growth in deposits, offset to some extent by higher growth in loans & advances amid the pandemic

Over FY17-FY21, NIC Asia has recorded robust growth in its deposits with compounded annual growth rate (CAGR) of 36% boosted by substantial expansion of its branches, which increased from 119 at the end of FY17 to 356 at the end of FY21. NIC Asia's deposits grew 42% y-o-y to Rs. 300,252 Mn in FY21. Similarly, the bank's loans & advances have also grown at a similar pace, slightly higher even, with a CAGR of 38% over FY17-FY21. NIC Asia's total loans & advances stood at Rs. 264,840 Mn at the end of FY21, up 52.43% y-o-y. Significant increase in loans & advances in such a short span can raise concerns in the asset quality and elevates risks of possible bulk crystallization of GNPLs. However, the bank's credit policy remains strong, as demonstrated by the historical low levels of GNPLs. Furthermore, the growth trend has moderated in H1FY22 – NIC Asia's loans & advances grew 3.25% but deposits declined 0.30% over FY21. Deposits in H1FY22 were impacted by the liquidity issues in the country's economy amid lower remittance, increasing balance of payment deficit, and reduced government expenditure.

Good profitability and sustained growth in total income and net profit in FY21; continued growth in H1FY22 despite industry-wide slowdown

During FY21, NIC Asia's total income grew 8.05% y-o-y to Rs. 25,912 Mn on account of rise in interest income by 13.70% y-o-y owing to the sustained growth in loans & advances over FY20-FY21. Consequently, NIC Asia's net interest income had increased by 21.34% y-o-y to Rs.9,228 Mn during FY21. On the operational efficiency front, operating expenses increased by only 3.65% y-o-y to Rs.5,547 Mn during FY21. Higher net interest income and lower growth in operational expenses led to the bank reporting 5.18% growth in PAT during FY21 of Rs.3,259 Mn. The growth trend continued during H1FY22 - bank's total income increased by 40.09% y-o-y to Rs.16,399 Mn backed by growth in interest income by 43.23% y-o-y to Rs. 15,030 Mn. Similarly, non-interest income of the bank also increased by 12.88% y-o-y to Rs.1,369 Mn during H1FY22 mainly due to higher fees earned during the period. Although interest expenses increased even more, by 49.51% y-o-y, during H1FY22 on account of increase in deposit rate resulting in a higher cost of funds of 7.06% during H1FY22 (H1FY21: 5.30%), the bank was still able to report a growth of 32.81% y-o-y in its net interest income to Rs.5,242 Mn

during H1FY22. Growth in both interest income and non-interest income absorbed the growth in interest and operational expenses leading to the bank reporting 16.57 y-o-y growth in its PAT, which was Rs.2,402 Mn during H1FY22 - second highest in the industry.

Diversified loan portfolio, concentration towards Retail and SME portfolio

NIC Asia has diversified portfolio distribution across sectors with higher lending of around 20.52% of total loans & advances as on January 14, 2022 (July 15, 2021: 20.79%) towards wholesaler & retailer sector. NIC Asia's loans & advances portfolio, however, remains concentrated towards retail and SME portfolio by design. Retail portfolio accounted for around 53% and SME for around 30% of the bank's loans & advances as on July 15, 2021, which increased slightly to 56% and 32%, respectively, as on January 14, 2022. Bank adequately lends to the deprived sector: 7% as on July 15, 2021 and 6% as on January 14, 2022.

Healthy CASA mix in line with industry average although some moderation during FY21-1HFY22

NIC Asia has historically maintained a healthy CASA mix in its total deposits. NIC Asia's CASA mix in its total deposits over FY19-FY21 has been around 40%, in line with the industry average of around 40%-43% during this period. However, CASA ratio declined to around 37% during FY21 and H1FY22 due to higher fixed deposits. Furthermore, CASA deposits were lower in H1FY21 industry-wide with lower proportion of current deposits as compared to previous quarters, resulting in lower CASA ratio overall for the industry of around 40% as on January 14, 2022.

Key Rating Weaknesses

Moderate capitalization a key concern as post-pandemic recovery remains largely unpredictable

Over FY19-FY21, the bank's capitalization levels declined to below industry average due to relatively higher pace of credit growth vis-à-vis capital accretion amid an aggressive growth model adopted by the bank during this period. As on mid-July 2021, NIC Asia's overall CAR was at 12.47% and Common Equity Tier I (CET-I) was at 7.36%, with thin cushion against the minimum regulatory requirement of 11% and 7%, respectively. Lower capitalization levels could limit a bank's ability to absorb losses, should they materialize, esp. given the uncertainty surrounding credit recovery amid the intermittent waves of the covid19 pandemic. However, NIC Asia's overall CAR and CET-I ratio improved to 12.74% and 8.01% as on mid-February 2022, respectively, aided majorly by a more restrained credit growth leading to decline in the bank's total risk weighted exposure. Capitalization levels are likely to improve further by the end of FY22 boosted by accretion of profits to reserves coupled with consolidation of the bank's loans portfolio. Improvement in capital adequacy indicators remains a key rating sensitivity.

Moderate liquidity profile

NIC Asia has moderate liquidity profile with positive cumulative mismatches as of January 14, 2022 due to well matched tenure of assets and liabilities. Although the assets and liabilities show mismatches in the 91-180 days and 271-365 days buckets on account of lesser advances due in contrast to liabilities maturing during these periods, cumulative mismatch remains positive. NIC Asia had maintained SLR of 17.27% as on July 15, 2021 vis-à-vis regulatory requirement of 10%. SLR has declined slightly to 15.62% as on January 14, 2022. However, the bank's net liquidity had dipped to 18.92% as on January 14, 2022, which was below the regulatory requirement of 20%. Net liquidity has improved to 20.09% as on February 12, 2022, which is within the norms of NRB.

Intense competition

Currently there are 27 Commercial Banks, including three major state-owned banks, operating with total 4,856 branches all over Nepal (based on monthly statistics published by NRB for mid-January 2022). NIC Asia had 358 branches along

with head office as on same date. Industry (Class 'A' Commercial Banks) had achieved total interest income of Rs. 193,217 Mn during H1FY22 with Rs. 69,353 Mn net interest income; NIC Asia's share on interest income was 7.68% and 7.28% on net interest income for the same period. These market shares of NIC Asia have slightly increased from 7.22% and 7.00% for interest income and net interest income during FY21, respectively. 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. 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 4.4% from earlier 5% via Monetary Policy issued by NRB, for FY21. Due to increased capital, banks are facing investable amount deficit to grant new loans and advances. And decreased weighted average interest rate spread together with growing competition will be responsible for decreasing net interest margin thereby impacting profitability.

About the Bank

NIC ASIA Bank Limited (NIC Asia) is "A" Class Licensed Institutions from Nepal Rastra Bank (NRB) Around 93.5% of the total shareholding of the Bank is held by individuals and around 6.5% by corporate entities (other than GoN and Licensed Institutions) as on July 15, 2021; among which 51% belongs to promoter group shares and 49% belongs to general public. The Bank has three wholly owned subsidiary companies operating within the territory of Nepal. One of them is NIC ASIA Capital Limited (incorporated to undertake Merchant Banking activities), other is NIC ASIA Laghubitta Bittiya Sanstha Limited (Microfinance) and NIC Asia Securities.

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About CARE Ratings Nepal Limited:

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