

## Kamana Sewa Bikas Bank Limited

### Rating

Facilities	Amount (Rs. in Million)	Rating <sup>1</sup>	Rating Action
Issuer Rating	NA	CARE-NP BB+ (Is) [Double B Plus (Issuer Rating)]	Reaffirmed

CARE Ratings Nepal Limited (CRNL) has reaffirmed issuer rating of 'CARE-NP BB+ (Is)' to Kamana Sewa Bikas Bank Limited (KSB). Issuers with this rating are considered to offer moderate risk of default regarding timely servicing of financial obligations, in Nepal.

### Detailed Rationale & Key Rating Drivers

The rating assigned to KSB continues to be constrained by its below average asset quality, modest liquidity profile, and moderate concentration over top 20 depositors. The rating is further inhibited by intense competition among BFIs and exposure to regulatory risk related to banking industry. The rating also factors in declining trend in capitalization level of bank in FY23 (Unaudited, FY refers to the twelve-month period ending mid-July). The rating, however, continues to derive strength from KSB's long track record of operations with experienced board and management team, growing and diversified advances portfolio, and increase in investment portfolio. The rating also draws strength from the bank's moderate Current Account Saving Account (CASA) deposits level and relatively steady financial performance during FY23. *Going forward, the ability of the company to continue its growth momentum while improving asset quality and capital adequacy ratio and its ability to manage the impact of any regulatory changes will be the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

##### Below average assets quality

KSB's asset quality continued to stand weaker than industry average in FY23. It reported Gross Non-Performing Loans (GNPL) ratio of 2.98% at the end of FY23 (industry average: 2.49%), increasing from 2.31% at the end of FY22 (industry average: 1.36%). The bank's gross NPL in absolute amount increased to Rs. 1,374 Mn as on mid-July 2023 from Rs. 1,095 Mn as on mid-July 2022. The increase was on account of industry-wide slippages and recovery challenges seen across various sectors, mainly in agriculture, manufacturing, hospitality, construction, etc., amid rising interest rates and slowdown in economic growth in the country, impacting borrowers' repayment ability. Out of total loans of Rs. 46,108 Mn as on mid-July 2023, delinquencies of more than 30 days amounted to Rs. 6,342 Mn (13.76% of total advances), which deteriorated from Rs. 1,932 Mn (4.37% of total advances) at the end of FY22.

##### Modest liquidity profile

KSB has a modest liquidity profile with negative cumulative balances as of mid-July 2023. It has maintained SLR of 18.50% as on July 16, 2023 and 16.13% as on July 16, 2022 vis-à-vis regulatory requirement of 10% and CRR of 4.04% and 3.13% at the last reporting week of FY23 and FY22 vis-à-vis regulatory requirement of 4%. Likewise, its Net Liquidity Ratio stood at 24.47% at the end of FY23, as compared to 23.30% in FY22 vis-à-vis regulatory requirement of 20%.

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

**Moderate concentration over top 20 depositors**

KSB's deposits from its top 20 depositors at the end of FY23 decreased to 16.04% of total deposits as compared to 19.74% of total deposits at the end of FY22. The top 20 depositors consist of all institutional depositors. Higher concentration on specific depositors normally increases re-pricing risks at times of interest rate volatility.

**Moderate CASA deposit ratio could lead to margin pressure**

KSB's CASA mix as on mid-July FY23 remains moderate despite slightly declining to 23.40% (industry average: 25.18%) from 23.66% as on mid-July FY22 (industry average of 25.62%). Due to decrease in CASA proportion, cost of deposit has increased to 9.37% at the end of FY23 as compared to 8.04% at the end of FY22. The ability of the company to maintain lower cost of funds will be critical as it would continue to provide a competitive advantage in the "base rate plus" lending rate regime.

**Declining trend in capitalization level over FY22-FY23**

KSB's overall capital adequacy ratio declined further to 12.29% at the end of FY23 from 13.28% at the end of FY22 (FY21: 13.93%). However, it continued to maintain a cushion over the regulatory requirement of 10%. Likewise, its Tier I Capital stood at 8.58% at the end of FY23, lower than 9.72% of at the end of FY22 (FY21: 10.02%), but above the regulatory requirement of 6%. KSB has seen an aggressive growth in its advances book over the last five years, resulting in sequential moderation in its core capitalization levels. The bank's ability to maintain an adequate cushion in its capital adequacy ratios is critical for its solvency and from the growth perspective.

**Competition from other banks and finance companies**

Currently, there are 17 development banks operating with total 1,128 branches all over Nepal (based on monthly statistics published by NRB for mid-July 2023). Out of that, KSB has 134 branches. Industry (Class "B" banks or Development banks) has achieved total interest income of Rs. 74,528 Mn in FY23 with Rs. 21,312 Mn net interest incomes; KSB's share on interest income and net interest income are both ~10% (Rs. 7,342 Mn and Rs. 2,165 Mn, respectively) for the same period. Despite being one of the well-established national development banks in the industry, it is challenging for KSB to maintain current market share and expand its business due to high competition among a large number of bank and finance companies conducting similar kind of businesses and offering wide banking services.

**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. From FY22 end, NRB has changed to Credit to Deposit (CD) ratio mechanism from existing Credit to Core Capital plus Deposit (CCD) ratio measures. CD ratio needs to be maintained below 90% from mid-July 2022 from earlier provision of 85% for CCD. Likewise, the risk weight 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 kept at 7.5% and repo rate decreased to 6.5% from 7% in the monetary policy issued by NRB for FY23. Such changes will likely put downward pressure on both lending and deposit interest rates of the bank over the near term.

## Key Rating Strengths

### **Experienced board members and management team supported by moderate geographical coverage**

KSB is a national level class "B" Development bank formed after the merger of Kamana Bikas Bank and Sewa Bikas Bank on August 4, 2017 (Pre-merger, both entities operating since 2007). KSB has a reasonable geographic presence in Nepal with 134 branches, one extension counter and 77 ATMs covering all 7 provinces as on mid-July 2023. It is a professionally managed bank under the overall guidance of the Board of Directors (BoD) led by Chairman Mr. Sudeep Acharya, who has worked in the banking sector for over 28 years. The senior management team is also composed of seasoned bankers and is led by CEO Mr. Dinesh Thakali, who has more than 20 years of banking experience.

### **Moderate growth in loans & advances and deposits with decent market share and diversified credit portfolio**

KSB's loan portfolio recorded a growth of 4.41% year-on-year at the end of FY23 over FY22 to Rs. 46,108 Mn. The overall Class-B banks' loan portfolio grew by 6.06% year-on-year in FY23. Similarly, KSB's deposit grew by 15.60% in FY23 as compared to industry's growth in deposits by 12.19%. It has 9.75% and 9.91% market share in terms of deposit base and loan portfolio, respectively, of the Class-B financial industry at the end of FY23 (9.92% and 10.22% respectively in FY22), based on monthly data published by NRB. KSB has a diversified loans portfolio across various industries/ sectors with highest lending of 25.10% at the end of FY23 for Consumable Loans (FY22: 6.61%) followed by 18.21% towards Wholesaler & Retailer Loans finance (FY22: 20.68%). Diversification helps the bank to maintain its assets quality and mitigate volatility risk in case of swings experienced in the economy.

### **Moderate financial performance in FY23**

During FY23, KSB's total income increased by 23.45% to Rs. 7,619 Mn supported by rise in interest income by 25.79% on account of sustained growth in loans and advances during the last few years. It was coupled with increase in yield on advances to 14.62% in FY23 compared to 12.96% in FY22. On the other hand, cost of deposits increased to 9.37% during FY23 from 8.04% during FY22 due to increased interest rates in the overall industry. Higher cost of funds was also in part on account of increase in proportion of fixed deposits as compared to the previous year. Due to higher cost of funds, KSB's Net Interest Margin (NIM) slightly declined to 3.54% in FY23 from 3.59% in FY22. Likewise, the total operating expenses increased by 4.46% in FY23 to Rs. 2,165 Mn compared to Rs. 1,993 Mn during FY22 on account of increase in the number of branches and increase in other operating costs. Also, KSB reported a decline in its Return on Total Assets (ROTA) to 0.70% in FY23 from 1.06% in FY22 due to growth in its total assets by 4.63% in FY23 against a 26.93% decline in its PAT.

### **Growing investment portfolio in FY23 and low portfolio concentration among top borrowers**

KSB's total investment recorded a growth of 26.50% to Rs. 7,920 Mn at the end of FY23 from Rs. 6,260 Mn at the end of FY22. Total investments include investment in government bills/ bonds of Rs. 1,055 Mn (FY22: Rs. 487 Mn), NRB bonds of Rs. 6,220 Mn (FY22: Rs. 5,521 Mn), and corporate shares (& others) of Rs. 645 Mn (FY22: Rs. 253 Mn) at the end of FY23.

KSB's lending to top 20 group and individual borrowers was 3.68% and 7.05%, respectively, as compared to 0.95% and 6.47%, respectively, at the end of FY22. Low concentration over top borrowers helps banks to avoid significant impact on their asset quality if any big borrower defaults on their loan.

**About the Company**

Kamana Sewa Bikas Bank Limited (KSB) is a national level class "B" Development bank formed after the merger of Kamana Bikas Bank Limited (established in FY07) (National level development bank) and Sewa Bikas Bank Limited (established in FY07) (10 district level development bank) on August 04, 2017. At the end of FY23, KSB has Rs. 3,281 Mn paid up capital, which is distributed among promoters and public shareholders in the ratio of 51:49.

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