

## Tinau Development Bank Limited

### ICRA Nepal assigns [ICRANP] IPO Grade 4 to the proposed Equity Share (Rights Issue) of Tinau Development Bank Limited

Facility/Instrument	Issue Size	Grading Action (January 2016)
Rights Share Issue	NPR 54.62 million	[ICRANP] IPO Grade 4 (Assigned)

ICRA Nepal has assigned an “[ICRANP] IPO Grade 4”, indicating below-average fundamentals to the proposed rights issue amounting to NPR 54.62 million of Tinau Development Bank Limited (hereinafter referred to as Tinau). ICRA Nepal assigns IPO grading on a scale of IPO Grade 1 through IPO Grade 5, with Grade 1 indicating strong fundamentals and Grade 5 indicating poor fundamentals. For the Grading categories 2, 3 and 4, the sign of + (plus) appended to the Grading symbols indicate their relative position within the Grading categories concerned. Thus, the Grading of 2+, 3+ and 4+ are one notch higher than 2, 3, and 4, respectively. Tinau is proposing to come out with 25% rights issue of 546,192.5 numbers of equity shares of face value NPR 100/- each to be issued to the existing shareholders at par. The proposed issue is being made in order to augment the capital base to support the future growth plans of the bank.

The grading factors in Tinau's experienced management team, moderate track record (operating since FY07), and healthy portfolio growth (CAGR<sup>1</sup> of ~36% over past 5 years although on a small base vs 24% for development bank industry). Bank's adequate franchise, moderate capitalization profile (CRAR of 11.92% as on mid Oct-15<sup>2</sup>) and low capital adjusted credit deposit ratio (~69% as on mid Oct-15) is expected to provide Tinau with adequate growth opportunities.

The grading is however constrained by high geographical concentration risks (>70% of business is concentrated within one district), modest scale of operations (asset base of NPR 2.9 billion as on Oct-15), and weak competitive positioning (resulting from high cost of funds and stiff competition from established BFs in the region). ICRA also takes note of buildup of delinquencies<sup>3</sup> during the last few months on account of uncertain operating environment created by ongoing political turmoil in the southern plains of the country impacting the overall economy and repayment capacity of the borrowers. On account of the same, Tinau witnessed deterioration in earnings profile during Q1FY16 (RoA of 1.15% during Q1FY16 as compared to 1.75% during FY15) and the asset quality could also be impacted going forward. However, Tinau reported fair asset quality as on Oct-15 (gross NPL of 0.03%). While assigning the grading ICRA Nepal has also factored in Tinau's capital base being lower to revised regulatory capital framework to be complied by FY17, lack of Institutional promoters, and relatively weaker borrower profile compared to commercial banks.

Nonetheless, the grading also factors in regulatory arbitrage available with 'Schedule B' Development Banks compared to 'Schedule A' commercial bank-in the form of lower absolute capital requirements and lower CRR/SLR<sup>4</sup> requirements. Going forward, Tinau's ability to scale up its operations ensuring efficient utilization of proposed capital raising through rights issue, maintain its profitability profile and manage the delinquency levels would have a bearing on the overall financial profile.

The credit portfolio of Tinau has grown at a CAGR<sup>1</sup> of ~36% over past 5 years ending mid July 2015 (vs. 24% growth in development bank industry). The healthy credit growth has been supported by the bank's adequate franchise (11 branches across 3 licensed districts), and competitive rates offered for advances. The credit portfolio of NPR 1,922 million as of Oct-15 primarily comprises business loans (41%), personal loans (24%), housing loans (14%), hire purchase loans (8%), agriculture loans (4%) among others. Tinau's

<sup>1</sup> Compounded annual growth rate

<sup>2</sup> Mid-Oct-15 data are unaudited

<sup>3</sup> Delinquent loans on mid-Oct-15 accounted for 4.57% of total loans vs. 0.71% in mid-July-15.

<sup>4</sup> Cash Reserve Ratio/ Statutory Liquidity Ratio



credit concentration remains moderate (top 20 borrower groups accounting for 14.22% of total loans on Jul-15) and fares better to most of the peers operating in same geography.

The bank reported gross NPLs<sup>5</sup> of 0.01% on Jul-15 (vs. 3.58% for development bank industry). However, post July-15 Tinau has witnessed some stress in recoveries on account of elongated strikes in terai region, resulting in an increase in the delinquency levels. Delinquent loans on mid-Oct-15 accounted for ~5% of total loans vs. ~1% on mid-July-15, with higher delinquencies in business loans segment as on mid-Oct-15 (~9% loans are delinquent in business loan segment). This could impact Tinau's asset quality profile going forward. Although, the regulator has provided temporary relaxations in NPL recognition norms factoring in the strike; Tinau has not availed the relaxations while reporting the NPLs of 0.03% in Oct-15. Nevertheless, portfolio vulnerability remain high vs. commercial banks due to inferior borrower profile and assessed income based lending, which could lead to volatility in asset quality indicators. Although Tinau's portfolio was not impacted directly by the earthquake (Apr-15), the exposures in unaffected geographies/segments could witness some stress due to overall moderation in economic activity as well as linkage among businesses/borrowers.

As for funding profile, Tinau's cost of funds (6.61% for FY15 vs. development bank industry average of 6.20%) remains moderate. The cost of deposits has witnessed sharp decline over recent years partly aided by improvement in deposit<sup>6</sup> mix of Tinau; enhancing the competitive positioning of the bank. Tinau has a healthy proportion of low cost CASA<sup>7</sup> deposits (~57% as on Jul-15 as compared to development bank industry average of ~53%) and a granular deposit base (top 20 depositors comprise 9.51% of total deposits on Jul-15). Adequate capitalisation level and low CD ratio (~69% as of Oct-15), on account of high growth in deposits amidst low demand for fresh credit in recent past, provide adequate room for credit growth provided the ongoing turmoil resolves soon and economic activity picks up. Going forward, the ability of Tinau to maintain the deposit profile will have a bearing on overall competitive positioning.

Tinau reported profit after tax (PAT) of NPR 41 million during FY15 (corresponding to return on net worth of 16.89% and return on assets of 1.75%) vs. NPR 30 million during FY14 (corresponding to return on net worth of 16.59% and return on assets of 1.63%). Tinau's profitability was primarily supported by healthy NIMs (NIMs were 4.24% in FY15) and low provisioning expenses. Amidst the challenging backdrop during Q1FY16 bank reported PAT of NPR 8 million (corresponding to a return on net worth of 12.17% and return on assets of ~1.15%). The deterioration during Q1FY16 was on the back lower cash recoveries<sup>8</sup> from accounts impacted by ongoing strikes. Going forward, the profitability profile of the bank will be dependent on its ability to manage delinquencies; the same however remains a challenge given the expected impact of elongated strikes on the repayment ability of borrowers.

Tinau's CRAR<sup>9</sup> stood at 11.79% on Jul-15 (11.92% as of Oct-15) as against minimum regulatory requirement of 11% for class B banks; with tier I capital of 10.95%. The proposed rights issue along with the internal accruals would help bank maintain adequate capitalization over the medium term. However, monetary policy of FY 2015-16 has announced that 3-district level Development banks are required to increase their paid-up capital to NPR 500 million within FY17. Tinau has a capital of NPR 218 million as of mid-Oct-15 and the same is expected to increase to NPR 273 million after proposed right issues (assuming full subscription). Bank would explore mergers with relatively smaller BFIs and/or retention of profits from FY15-16 and FY16-17 to meet the revised regulatory capital requirements. Finding adequate sources to meet the elevated regulatory requirement would remain a key challenge for the bank.

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<sup>5</sup> Non-performing loans

<sup>6</sup> CASA deposits improved from 48% in Jul-13 to 60% in Oct-15.

<sup>7</sup> Current and Saving accounts

<sup>8</sup> Recognition of Income for Bank & financial institution is cash basis as per regulation

<sup>9</sup> Capital to risk weighted assets ratio



## Company Profile

Tinau Development Bank Limited (Tinau) started its commercial operation from 1st November 2006. It is licensed by NRB as a 3-district class B development bank to conduct banking transactions within three districts (Chitwan, Rupandahi & Nawalparasi). The bank is promoted by 29 individual from different professional backgrounds. Mr. Pradeep Kumar Shrestha is the Chief Executive Officer of Tinau. The bank's registered office is in Butwal sub-metropolitan city in Rupandehi district, which is also the Head Office.

Tinau has presence in three districts of the country through its 11 branches and four ATMs. The bank has market share of about 1% in terms of deposit base and 0.94% of total advances of development banks in Nepal as on mid-Jul-2015. Tinau reported a profit after tax of NPR 40.88 million during 2014-15 on an asset base of NPR 2,681 million as on Jul-15 against profit after tax of NPR 30.29 million during 2013-14 on an asset base of NPR 1,990 million as on Jul-14. During Q1FY15-16, Tinau also reported profit after tax of NPR 7.96 million on an asset base of NPR 2,852 million on mid-Oct-15. Tinau's gross NPL stood at 0.03% and CRAR at 11.92% as on mid-Oct-15. In terms of technology platform, Tinau has implemented Pumori IV in all of its branches.

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