Sanima Bank Limited

ICRA Nepal assigns [ICRANP-IR] A- rating to Sanima Bank Limited and upgrades subordinated debenture rating of the bank from [ICRANP] LBBB+ to [ICRANP] LA-; "rating watch with negative implications" has been removed

Facility/Instrument	Amount	Rating Action (July 2017)
Issuer Rating	NA	[ICRANP-IR] A- (assigned)
Subordinated Debenture Program	NPR 370 Million[1]	[ICRANP] LA- (upgraded)*

"rating watch with negative implications" removed.

ICRA Nepal has assigned rating of **[ICRANP-IR] A-** (pronounced ICRA NP Issuer Rating A minus) to Sanima Bank Limited (Sanima). Entities with [ICRANP-IR] A- rating are considered as adequate-credit-quality rating assigned by ICRA Nepal. The rated entity carries average credit risk. The rating is only an opinion on the general creditworthiness of the rated entity and not specific to any particular debt instrument.

ICRA Nepal has also upgraded the rating of subordinated debentures of NPR 370 million of Sanima from **[ICRANP] LBBB+** (pronounced ICRA NP L Triple B Plus) to **[ICRANP] LA-** (pronounced ICRA NP L A minus). Subordinated debenture rating A- is one notch higher than BBB+. Instruments with this rating are considered to have adequate degree of safety regarding timely servicing of financial obligations. Such instruments carry low credit risk. The rating has been removed from "rating watch with negative implications".

Subordinated debenture rating for Sanima was put on watch with negative implications in April 2015, pending detailed assessment of the impact due to the earthquake on bank's credit and financial profile. The rating was continued under watch amid assets quality concerns emanating from blockade in subsequent months. While removing the rating from watch and upgrading it, ICRA Nepal takes into consideration Sanima's demonstrated ability to achieve scale growth with adequate control, maintaining superior assets quality and adequate profitability levels.

The rating action factors in the bank's ability to consistently maintain its assets quality (Gross NPLs ~0.01% as on Mid-Jul-17, with total delinquent loan less than 2.5%) on a growing scale of operation. The rating also factors in the improvement in funding mix, decline in portfolio concentration among top accounts and strong capitalisation profile (CRAR of ~16% as on Mid-Jul-17) aided by recent equity injection by the shareholders. The rating also remains supported by established underwriting norms and risk management framework being practiced within the bank. The rating action also factors in the improvement in Sanima's market positioning due to business growth in recent years. Despite its short track record as a class A commercial bank, Sanima has grown in scale at a healthy pace and remains comparable to the banks with relatively longer history. Incremental growth prospects of the bank remain supported by strong capitalisation, comfortable CCD (credit to deposit ratio adjusted for capital) ratio of ~76% as on mid-Jul-17 and experienced management team.

The ratings are however constrained by Sanima's limited track record as a class A commercial bank and rapid portfolio growth in shorter timeframe; especially during low interest rate regime of FY13-FY16. The unseasoned credit books could come under stress given recent rise in banking interest rates. Sanima's franchise network also remains moderate vis-à-vis peers and could affect the competitive positioning, especially considering the retail/SME oriented credit portfolio. Sanima's deposit profile remains inferior to commercial bank average in terms of current and savings account (CASA) proportion (though better than many new generation private sector commercial banks). Resulting high cost of deposits could affect the base rate of the bank and weaken its competitive positioning going forward, especially in the "base rate plus" lending rate regime implemented by Nepal Rastra Bank (NRB). Risks also emanate from the

[1] Although the original rating outstanding was for NPR 700 million, Sanima raised only NPR 370 million as Banks were required to raise their paid-up capital by four-fold after the monetary policy announcement in July 2015.

acquisition[2] of class B development bank (albeit with small scale of operation) with relatively moderate underwriting norms vis-à-vis commercial banks. The rating is also constrained by uncertain operating environment that the banks in Nepal are currently facing.

Sanima's credit portfolio has grown organically[3] at a healthy pace of CAGR ~37% during FY14-9MFY17, albeit on a low base. The bank has steadily focussed on retail and SME sector to generate credit growth during past 2-3 years. Focussed growth along retail segment has eased the credit concentration among top borrowers despite sizeable credit growth in recent years. As on mid-April 2017, Sanima's credit portfolio primarily comprised of retail loans (45%), SME/Business loans[4] (23%), corporate loans (21%), project financing loans (7%) and deprived sector loan (4%). Incremental credit growth is likely to remain supported by Sanima's equity injection plan to meet revised paid up capital of NPR 8 billion. However, the bank's ability to achieve the growth targets along with commensurate control measures remains to be seen. Sanima has reported superior assets quality with gross Non-performing loans (NPLs) of 0.04% as on mid-April 2017 along with low delinquency level (~2% as on mid-April 2017). Although bank's ability to maintain good assets quality level remains a comfort, Sanima's higher than average concentration in vulnerable sectors[5] remains a concern especially in the current regime of rising interest rate.

Sanima's CASA deposit proportion grew from ~36% to ~47% during FY14-16. Improvement in CASA mix was supported by focussed approach of the bank towards boosting the retail savings deposit base. Sanima's CASA proportion has softened during 9MFY17 like most of the industry peers as the banks are focussing on term deposits to counter the deposit crunch situation and stabilize the funding profile. Although, CASA proportion of Sanima remains inferior to commercial bank average, it remains stronger to most of the new age private sector commercial banks. Cost of deposits of Sanima stood at 4.62% during 9MFY17, ~100 bps higher than commercial bank average. Cost of deposits for Sanima has increased in recent period (5.39% for FY17) due to deposit crunch in banking industry. CCD ratio of Sanima bank remains comfortable despite the moderation in deposit growth vis-à-vis credit growth in recent years. Nonetheless, incremental credit growth is likely to remain driven by the bank's ability to raise incremental deposits. Stability of deposit is comforted by fair proportion of retail deposits and relatively lower deposit concentration among top accounts.

As for profitability, Sanima's return on net worth (20-22%) surpassed commercial bank average during FY16 and 9MFY17, following years of high business growth and resulting scale economies. Profitability remains supported by fair Net Interest Margin (NIMs) (~3.60% of average total assets (ATA)) on growing asset base. NIMs was supported by healthy yield on advances on retail/SME dominated lending portfolio and healthy rate of credit mobilisation (CCD ratio of 75-80% during past 6-12 months). Profitability during the period was also supported (albeit moderately) by non-interest income (~1.12%), moderation in operating expense ratio with growth in scale and low credit provision expense ratio (~0.25%). Sanima's average return on net worth for FY17 has diluted (to ~18%) after capitalisation of fresh equity[6] during Q4FY17; yet remains fair and better to most of the new generation banks. Going forward, bank's profitability will depend on its ability to achieve targeted growth by managing required funds and maintain assets quality on current and incremental credit portfolio.

Sanima has operated with healthy capital cushion over the regulatory minimum since its upgradation into a class A commercial bank in 2012. The bank's capital to risk assets ratio (CRAR) stood at 13.20%, as on mid-April 2017; comfortable vis-à-vis regulatory minimum of 11% under prevailing Basel III norm. Capitalisation of fresh equity during Q4FY17 has further strengthened the capital adequacy ratio to ~16% as on mid-July 2017. Sanima's tier I capital (11.64% as on mid-April 2017) remains well above 7.50% to be maintained by mid-July 2017 and 8.50% to be maintained by mid-July 2019 under the Basel

[2] Sanima acquired Bagmati Development Bank (1 district level class B Bank) in early 2017.
[3] Although Sanima acquired a 1-ditrict level Development bank in the interim, the portfolio addition was negligible.
[4] SME credit covers loan upto NPR 100 million; beyond that is corporate loans as per Sanima's internal classification.
[5] Mainly real estate loans and equated monthly payment based hire purchase loans.
[6] NPR 1,592 million is the final tranche of fresh equity injection in order to meet NPR 8 billion paid up capital mark.

III norms prescribed by NRB. Therefore, capitalization levels are expected to remain adequate to support Sanima's growth plans over the medium term.

Bank Profile

Sanima Bank Limited (Sanima) started its commercial operation from 2004 as national level development bank (Class B) and was upgraded into class A commercial bank in February 2012. Its head office is located at Naxal, Kathmandu. The bank is promoted by Non-Resident Nepalese (NRN) Businessman loosely affiliated under brand name Sanima Group. Major promoters of the bank included Mr. Arun Kumar Ojha (~13% shareholding), Mr. Tekraj Niroula (~8%), Dr. Niraj Govinda Shrestha (~6%), Mr. Jibanath Lamichhane (~6%), Mr. Binay Kumar Shrestha (~5%), etc. Mr. Bhuvan Kumar Dahal is the Chief Executive Officer of the bank. The bank's equity share is listed in Nepal stock exchange.

Sanima acquired Bagmati Development Bank Limited (BDBL) (1 district level Class B development bank) in early 2017 and started joint operation from 13th January 2017. The rationale for merger was to avail the tax benefits allowed by regulations for entities opting for merger/acquisition. Due to small scale of operations of erstwhile BDBL (~1% of Sanima's assets base at the time of acquisition), business synergies is likely to remain modest.

As on mid-April 2017, Sanima has presence throughout the country through its 45 branches (incl. Head Office) and 52 ATMs. Sanima has market share of about 2.34% in terms of deposit base and 2.51% of total advances of Nepalese Banking Industry as on mid-April 2017 (2.74% and 2.97% share respectively among the commercial banks). Sanima reported a profit after tax (PAT) of NPR 1,300 million during FY2016-17 over an asset base of NPR 70,019 million as on mid-July 2017 as compared to PAT of NPR 996 million during FY 2015-16 over an asset base of NPR 55,965 million as at mid-Jul-16. As of mid-July 2017, Sanima's CRAR stood at 15.55% and gross NPLs were 0.01%.

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