

Machhapuchchhre Bank Limited

ICRA Nepal assigns [ICRANP] LBBB- rating to subordinated bond programme of Machhapuchchhre Bank Limited

Facility/Instrument	Amount (NPR million)	Rating Action (June 2015)
Subordinated Bond Program	500	[ICRANP] LBBB- (Assigned)

ICRA Nepal has assigned rating of [ICRANP] LBBB- (pronounced ICRA NP L triple B minus) to subordinated bond programme of NPR 500 million of Machhapuchchhre Bank Limited (MBL). Instruments with this rating category are considered to have moderate degree of safety regarding timely servicing of financial obligations. Such instruments carry moderate credit risk. For the rating categories AA through to C, the sign of + (plus)/ - (minus) appended to the rating symbols indicate their relative position within the rating categories concerned. Thus, the Rating of BBB+ is one notch higher than BBB, while BBB- is one notch lower than BBB.

The rating factors in the MBL's long track record (operating since October 2000), adequate franchise¹ leading to average market positioning with ~2.75% share in Nepalese banking sector credit on mid-April-15, deposit profile with fair CASA² deposit proportion (43% of total deposits on mid-April-15), and experienced management team. ICRA Nepal expects moderate level of stress on MBL's asset quality and profitability profile expected over next 2-3 years due to damage caused by the earthquake in April 2015 and aftershocks. At this stage, exact quantum of damage is not ascertainable. ICRA will closely monitor the extent of damages on MBL's financial and solvency profile, in case damages turn out to be higher, the rating could move down.

As for impact on MBL's operations, MBL's branches in the earthquake affected areas accounted for ~45% of the credit portfolio and ~70% of the deposits as on April-15 however several of these businesses (end users of loans) are situated outside the earthquake affected areas due to which exact quantum of affected exposures and extent of damage could be restricted to certain sectors/segments³ accounting for ~1/3rd of MBL's loan book. Apart from stress in affected geographies/segments, exposures in unaffected geographies/segments could also witness some stress due to overall moderation in economic activity as well as linkage among businesses/borrowers.

ICRA Nepal has also noted that earthquake has not caused significant stress on MBL's deposits/liquidity profile⁴. Furthermore, recent activity in the stock market suggests that banks' ability to raise capital to absorb damages caused by earthquake is not significantly deterred.

As for capitalisation profile, MBL reported CRAR⁵ of 11.12% on mid-April-15⁶ and 10.63% in July-14) vs. 10% regulatory minimum requirements. In addition to the proposed subordinated debenture issue, the bank is also looking to raise capital through 20% rights issue in early FY16. The banks' ability to raise planned capital in a timely manner would have critical bearing on its ability to absorb damages arising out of earthquake and maintain comfortable solvency profile. The rating is also constrained by low non-interest income levels (~0.8% of ATA⁷) impacting diversity of earnings, relatively high deposit concentration (top 20 depositors accounted for 29% of total deposits on Jan-15), lack of institutional

¹ Franchise includes 51 branches and 69 ATMs as on Jan-15.

² Current & Savings accounts

³ Tourism, hydropower, real estate/construction, consumer loans, housing loans and loan book of micro finance entities

⁴ MBL's deposits were NPR 41.7 billion as on June 18, 2015 vs. NPR 41.5 billion as on April 13, 2015

⁵ Capital to risk assets adjusted ratio

⁶ Based on unaudited financials

⁷ Average total assets



promoter support, unstable political conditions and uncertain operating environment that banks in Nepal are currently facing.

MBL's credit portfolio of NPR 35,098 million on mid-April-15 accounted for ~2.75% of Nepalese banking industry credit. MBL's credit portfolio growth has remained high (CAGR of 34%) in past 3 years (after merger with Standard Finance- a class C finance company in July 2012). However, the credit growth over next 1-2 years is likely to get stunted on account of lack of credit demand following recent earthquake and moderation in economic activity however reconstruction drive would support credit growth to some extent. As on mid-April-15, the credit portfolio of the bank was primarily composed of large corporate loans (~52%), Retail loans (~36%) and Business/SME loans (~12%)⁸. The proportion of corporate loans has declined in recent years to the benefit of Retail & SME segments which grew from 37% on July-13 to 49% on April-15. MBL's retail portfolio growth remains healthy on account of home and vehicle loan which accounted for ~50% of retail loans and grew by >60% in 9MFY15. Increase in retail portfolio has also resulted in lower concentration among top borrowers (17% of credit accounted for by top 20 borrowers on mid-Jan-15), providing some comfort.

Assets quality of MBL has remained comfortable in past 12-18 months with Gross NPLs of 1.76% on April-15 and 1.78% in July-14, following accounting write-offs of loans in excess of NPR 1,400 million⁹ during the periods from FY11 to FY14. Similarly the solvency position remained comfortable with Net NPA/Net worth of ~9% on April-15. However, asset quality is expected to come under pressure going forward due to damage caused by earthquake, impacting borrowers' ability to make repayments in a timely manner.

MBL's reported CRAR was 11.12% on April-15 with tier I capital of 10.12%. The bank is looking to raise capital through subordinated debt of NPR 500 million in FY15 as well as through right issue of NPR 555 million in early FY 2016. The banks' ability to raise planned capital in a timely manner would have critical bearing on its ability to absorb damages arising out of earthquake and maintain comfortable solvency profile. However, modest profit levels in past and likely pressure in profit levels following the earthquake remains a challenge in internal capital generation.

MBL's profit levels have remained modest in past 5 years though improved modestly in FY14 and 9M FY15. In FY14, MBL reported PAT/ATA of 1.81% and PAT/Net worth of 14.5% as compared with FY11-FY13 average PAT/ATA of ~0.3% and PAT/Net worth of ~2.5%. MBL's profitability during these years were affected by high credit provisioning expenses (average of 1.5% of ATA during FY11-FY13). In FY14 and 9MFY15, the profitability of MBL was benefitted from high credit growth, improvement in NIMs (~3.2% of ATA) and CD ratio (~75%) coupled with lower credit provisioning expense (0.2% of ATA) and improvement in operating expense ratio (<2% of ATA) with balance sheet growth. Moreover, low level of MBL's non-interest income remains a drag on profitability as well as diversity of earnings. ICRA Nepal expects MBL's profitability profile to remain under pressure over next 2-3 years due to impact of devastating earthquake in 2015.

Bank Profile

Machhapuchhre Bank Limited (MBL) started its commercial operation from October 3, 2000 and is registered as "A" class Commercial Bank with Nepal Rastra Bank (NRB) - Central bank of Nepal. It was registered as first commercial bank with head office outside Kathmandu (in Pokhara city of western Nepal). Its head office (registered office) is located at Nayabazaar, Pokhara and its corporate office is in Lazimpat, Kathmandu. The bank is promoted by individual promoters from business background led by prominent Non-Resident-Nepalese (NRN) businessman Mr Upendra Mahato and family. Mr. Tulsi Gautam (former credit chief of Nepal SBI Bank) is the Chief Executive Officer of the bank. The bank's equity share is listed in Nepal stock exchange with total market capitalization of about NPR 15.5 billion as of mid-June 2015.

⁸ Corporate Loans: >30 million; SME loans: < 30million, towards a single borrower or related group of borrowers.

⁹ ~4% of April-15 total loans; writeoff includes loan of NPR 1,250 million towards a single borrower group.



MBL has presence across 31 districts of the country through its 51 branches including Head office and 69 ATMs. MBL is a medium size bank with market share of about 2.75% in terms of credit portfolio and 2.56% in terms of deposit base in Nepalese banking industry as on mid Jan-15. MBL reported a profit after tax of NPR 455 million during 2013-14 over an asset base of NPR 40,723 million as on Jul-14 as against profit after tax of NPR 149 million during 2012-13 over an asset base of NPR 30,296 million as on Jul-13. During 9M FY15, MBL reported PAT of NPR 440 million. MBL's CRAR was 11.12% and gross NPLs were 1.76% as on mid-April-15.

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