

## Nepal Bangladesh Bank Limited: Ratings reaffirmed

July 27, 2020

### Summary of rated facilities/instruments

Facility/Instrument	Amount	Rating Action (July 2020)
Issuer Rating	NA	[ICRANP-IR] BBB+; reaffirmed
Subordinated Debenture Programme	NPR 2,000 Million	[ICRANP] LBBB+; reaffirmed

### Rating action

ICRA Nepal has reaffirmed the issuer rating of **[ICRANP-IR] BBB+** (pronounced ICRA NP issuer rating triple B plus) assigned to Nepal Bangladesh Bank Limited (NBB). The rating is considered to be of moderate credit quality. The rated entity carries a moderate credit risk. The issuer rating is only an opinion on the general creditworthiness of the rated entity and not specific to a particular debt instrument. The sign of + (plus) or – (minus) is appended to the rating symbols to indicate their relative position within the rating categories concerned.

ICRA Nepal has also reaffirmed the rating of **[ICRANP] LBBB+** (pronounced ICRA NP L triple B plus) assigned to the subordinated debenture programme of NBB. Instruments with this rating are considered to have a moderate degree of safety regarding the timely servicing of financial obligations. Such instruments carry moderate credit risk.

### Rationale

The rating action continues to factor in NBB's strong institutional promoters, with ~41% stake of IFIC Bank<sup>1</sup> and representation in NBB's board through three directors. NBB's established track record (operating since 1994), diversified network, along with the experienced/stable management team and its adequate capitalisation profile are expected to provide it with adequate growth opportunities. The ratings also take into consideration the bank's healthy net interest margins (NIMs) and strong fee-based income leading to adequate return on assets (1.69% for 9M FY2020). NBB's balanced portfolio mix, with ~38% SME loans, followed by ~32% corporate loans and ~30% retail loans, also remains a rating positive.

Nonetheless, the ratings remain constrained by the stress seen in the bank's asset quality in the recent periods with rise in the 30+ days delinquencies (DPD) to ~13% as of mid-April 2020, including non-performing loans (NPLs) of 2.76% (30+ DPD was ~4% as of mid-July 2018). ICRA Nepal also takes note of the bank's increased pace of credit growth in FY2019 (~29%, remaining much higher to ~18% industry growth), which remains a rating concern. However, the pace of growth has moderated to ~16% in 9M FY2020. The ratings also remain impacted by the bank's relatively smaller asset base in relation to its age and its market positioning as one of the smaller players in the industry with ~2% share in industry credit and deposits. The ratings also consider the risks emanating from a sizeable non-fund-based business, which remains almost at par with the fund-based portfolio. NBB's relatively weaker deposits profile with low proportion of stable/ low-cost current and savings accounts (CASA), leads to a relatively higher cost of funds. This, along with high deposit concentration risks (~35% from top-20 depositors as of mid-April 2020), also remain key rating concerns. Further, the economic impact of Covid-19 could impair the repayment capability of a sizeable chunk of borrowers and hence impact the asset quality indicators for the banking sector over the medium term. However, the recent Monetary Policy announcement is likely to provide some support. Going forward, the bank's ability to control fresh slippages and improve the portfolio granularity while maintaining comfortable capitalisation profile would remain crucial. Also, its stance in attaining sustainable portfolio growth, while maintaining adequate profitability amid the regulatory changes would remain a key monitorable.

### Key rating drivers

#### Strengths

**Long track record; adequate franchise leading to balanced portfolio mix** – NBB has a long and established track record in the industry with its operations having started from 1994. The bank has adequate presence with 96 branches and 80 ATMs as of mid-April 2020. This has aided it in maintaining a balanced portfolio mix with ~38% SME loans, followed by ~32%

<sup>1</sup> IFIC Bank is one of the oldest and established banks of Bangladesh with a long track record of over 37 years in commercial banking. The Government of the People's Republic of Bangladesh holds ~33% stake in IFIC Bank.

corporate loans and ~30% retail loans. Though the dependence within top corporates remains high at ~20% among the top-20 groups as of mid-April 2020 (110% of tier-I capital; 102% last rating), the credit concentration remains relatively moderate among peers.

**Presence of strong promoters and experienced board/management** – ~41% promoter stake in NBB is held by the IFIC Bank of Bangladesh, which itself has a long track record (~38 years) in banking. The promoter bank had extended support in the past (through increased stake from 10% earlier), when NBB was going through a troubled stage. The experienced background of directors, including representatives of IFIC, and the experienced/stable management team remain rating positives.

**Adequate profitability profile** – NBB's earnings profile remained adequate owing to its healthy NIMs at 4.18% in FY2019, however, slightly declining to 3.60% in 9M FY2020 on account of the regulatory constriction in lending spreads. The bank's strong fee-based income (1.89% of the average total assets (ATA) for FY2019), arising from its sizeable non-fund-based business, also supports the profitability. Nonetheless, its fee-based income has also witnessed a decline in 9M FY2020 to 1.59% of ATA. This was mainly on account of the slowdown in construction activities, which impacted its key customer segment (construction contractors). NBB's operating expense ratio generally remains on a slightly higher side at 2.08% of ATA in 9M FY2020 and hence remains a drag on its profitability. Given the bank's moderate asset base, the return on assets (RoA) at 1.69% in 9M FY2020 remained better to the industry average of 1.57%. The return on net worth (RoNW), however, remains moderate at ~10.6% in 9M FY2020 due to sizeable capital charge for relatively low yielding non-fund based business. Going forward, the bank's ability to maintain adequate NIMs and manage the asset quality would have a strong bearing on its profitability profile.

**Adequate capitalisation profile** – NBB's reported capital to risk-weighted assets ratio (CRAR) of 12.88% and tier-I capital of 10.36% as of mid-April 2020 remain adequate against the minimum regulatory requirement of 11% and 8.5% respectively, as per the prevailing BASEL-III norms implemented by the Nepal Rastra Bank (NRB, the regulator). The bank's solvency profile (net NPA/net worth) remains stretched at ~5% as of mid-April 2020; any large slippages would have a bearing over the bank's financial profile. Given NBB's moderate internal accruals and profit retention as per business growth needs in the past, capitalisation levels are expected to remain adequate to support the management's growth plans while maintaining comfortable solvency profile. ICRA Nepal also expects timely equity support from the parent bank, if required.

## Challenges

**Stressed assets quality** – The bank's asset quality has witnessed increased stress in the recent periods with NPLs rising to 2.76% in mid-April 2020 from 1.78% as of mid-January 2019. The 30+ days delinquencies have also sharply increased to ~13% (from ~4% levels earlier) which increases concerns over its asset quality. With recent fresh slippages, the provision cover remains moderate at ~62% as of mid-April 2020. NBB's ability to reduce the delinquency/NPLs would remain a key rating factor. Any slippages leading to depletion in capitalisation levels could have a bearing on the ratings assigned.

Going forward, the asset quality of the banking sector, including NBB, is expected to witness some moderation due to a decline in the repayment capability of borrowers amid the ongoing pandemic. The pickup in economic activities in the post-lockdown era remains to be seen and the same would have a bearing over the asset quality outlook. Additionally, banks would have to carefully analyse the impact on the borrower's cash flow streams and provide the rescheduling/moratorium, accordingly, as announced by the recent Monetary Policy. In lack of prudent deferrals of loans and arbitrary addition of loans, the asset quality impact is likely to surface after some lag.

**Spiked credit growth and high non-fund based business** – NBB's credit grew by ~29% in FY2019 after low growth compared to the industry in earlier few years. Though the growth rate moderated to ~16% in 9M FY2020 (industry growth at ~19%), the build-up in asset quality stress recently, after the increased credit growth, remains a concern. The bank's credit portfolio of ~NPR 61 billion as of mid-April 2020 accounted for ~2% of the industry credit, which is low compared to the bank's track record. Also, the share of its non-fund business remains high at ~97% of the fund-based portfolio as on the same date, which could increase the portfolio vulnerability amid the expected economic slowdown.

**High deposit concentration and lower CASA** – The bank's deposit concentration on the top-20 accounts continues to remain high, albeit with slight moderations since the last rating (~35% as of mid-April 2020; 38% last rating). Though the CASA deposits portion remains slightly low at ~38% compared to ~41% for industry as of mid-April 2020, rates offered herein are relatively higher. Hence, the bank's cost of deposits at 7.15% for 9M FY2020 remained higher than the industry

average of 6.32% for the same period. Improving the deposits mix, concentration and cost would remain key challenges for the bank over the medium term.

**Analytical approach:** For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below.

**Links to applicable criteria:**

[Bank Rating Methodology](#)

[Corporate Debt Rating Methodology](#)

### Bank Profile

Nepal Bangladesh Bank Limited (NBB) was incorporated in 1994 as a joint venture with IFIC Bank of Bangladesh. IFIC Bank holds ~41% promoter shares in NBB while the major chunk of the remaining promoter shares (~11%) is held by individuals from the NB Group. The rest of the bank's shares are held by the public. All three promoter directors of the bank, including the Chairman, are representatives of IFIC Bank. NBB's shares are listed on the Nepal Stock Exchange. The registered and corporate office of the bank is located at Kamaladi, Kathmandu.

NBB has its presence across the country through its 96 branches, seven extension counters and 80 ATMs as of mid-April 2020. As on the same date, the bank had a market share of 1.98% in terms of deposit base and 2.15% of total advances of commercial banks. NBB reported a profit after tax (PAT) of NPR 1,620 million during FY2019 (YoY growth of ~42%) over an asset base of NPR 78,125 million as of mid-July 2019. For 9M FY2020, the bank reported a PAT of NPR 1,005 million over an asset base of NPR 80,496 million as of mid-April 2020. As on the same date, NBB's CRAR was 12.88% and gross NPLs were 2.76%. In terms of technology platform, NBB has implemented Pumori software across all its branches.

### Key financial indicators

Year Ended	Mid July 2017 (Audited)	Mid July 2018 (Audited)	Mid July 2019 (Audited)	Mid-April 2020 (Provisional)
<b>Operating ratios</b>				
Yield on average advances	10.19%	12.92%	13.52%	12.08%
Cost of deposits	5.06%	7.47%	7.36%	7.15%
Net interest margin/ATA	2.94%	3.33%	4.18%	3.60%
Non-interest income/ATA	1.79%	1.83%	1.72%	1.52%
Operating expenses/ATA	1.97%	1.99%	2.17%	2.08%
Credit provisions/ATA	0.03%	0.51%	0.51%	0.70%
PAT/ATA	2.32%	1.93%	2.32%	1.69%
PAT/net-worth	14.57%	10.32%	13.38%	10.59%
Gross NPAs	0.76%	1.27%	1.73%	2.76%
30+ days delinquencies		3.81%	2.40%	12.66%
<b>Capitalisation ratios</b>				
Capital adequacy ratio	15.10%	14.03%	13.75%	12.88%
Net NPAs/net worth	1.07%	2.04%	2.66%	5.05%
<b>Liquidity ratios</b>				
Total liquid assets/total liability	33.05%	29.19%	24.59%	19.79%
Total advances/total deposits	84.37%	88.07%	91.09%	97.79%

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## About ICRA Nepal Limited

ICRA Nepal Limited, the first credit rating agency of Nepal, is a subsidiary of ICRA Limited (ICRA) of India. It was licensed by the Securities Board of Nepal (SEBON) on October 3, 2012. ICRA Nepal is supported by ICRA Limited through a technical support services agreement, which envisages ICRA helping ICRA Nepal in areas such as rating process and methodologies, analytical software, research, training, and technical and analytical skill augmentation.

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For more information, visit [www.icranepal.com](http://www.icranepal.com)

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