Everest Bank Limited: [ICRANP-IR] AA- (assigned)

September 27, 2023

Summary of rating action

Instrument/Facility	Amount	Rating Action
Issuer Rating	NA	[ICRANP-IR] AA- (assigned)

Rating Action

ICRA Nepal has assigned issuer rating of [ICRANP-IR] AA- (pronounced ICRA NP issuer rating double A minus) to Everest Bank Limited (EBL). Issuers with this rating are considered to have high degree of safety regarding the timely servicing of financial obligations. Such issuers carry very low credit risk. The issuer rating is only an opinion on the general creditworthiness of the rated entity and is not specific to any debt instrument.

Rationale

The assigned rating factors in EBL's long track record of operation (since 1994), good ownership profile (including 20% equity stake from its joint venture (JV) partner Punjab National Bank-PNB)[1] and established system and processes partly resulting from technical support service agreement with the JV partner. The rating also factors in EBL's comfortable assets quality and solvency indicators (notwithstanding recent deterioration). EBL's conservative underwriting norms, its competitiveness in terms of the ability to offer finer lending rates and the bank's seasoned credit portfolio (given its slower-than-industry-average growth in the past) offers some comfort to the bank's incremental asset quality outlook; amid the current slowdown in economic activities and banking sector credit growth. The assigned rating also derives comfort from EBL's good capital cushion with CRAR of 13.3% (and tier I capital of ~11.2%) as on mid-July 2023 vs. regulatory minimum of 11% (and 8.5%). EBL's comfortable liquidity position with liquid assets/total liability ratio of ~30% and regulatory CD ratio of ~83% as of mid-July 2023 also remains rating positive. EBL maintains a good deposit profile with CASA proportion and cost of deposits generally comparable to the industry average[2], notwithstanding the bank's rise in average deposit costs in FY2023 because of higher growth in term deposit. Although profitability profile of the bank has been affected after the lowering of interest spread cap, EBL reported better than industry average return on net worth in FY2023; partly supported by improvement in net interest margins and controlled operating expense.

However, the ratings are constrained from the relatively high portfolio concentration of the bank (top 20 borrowers accounting for ~22% of the total loans and ~163% of Tier I capital and top 20 depositors accounting for ~22% of total deposits as of mid-July 2023). EBL has reported a relatively low non-interest income over the years, indicating limited revenue diversification which could affect profitability and internal capital generation during the period of weak NIMs. The incrementally stringent regulatory changes (new guidelines in working capital loans, NPL recognition in the case of related entities, etc) and its impact on fresh credit creation has created liquidity pressures across the borrower community and triggered a gradual rise in delinquencies across banks including EBL, which also remains a major rating concern at present.

Going forward, EBL's ability to maintain adequate capital and liquidity cushion amid the pan-Industry asset quality concerns will remain key rating sensitivities. Therefore, the bank's incremental delinquencies, credit growth and dividend policies will remain key rating monitorable. To that end, the bank's controlled cash dividend declaration out of FY2023 profit remains a positive.

1 Rated [ICRA] AA+(positive) by ICRA Ltd, India for Tier II Bonds

2 *Industry average CASA and cost of deposits ratio are generally skewed because of significantly higher CASA deposits/low cost of fund of few governments owned and foreign subsidiary banks.*

Key rating drivers

Credit strengths

Long track record, seasoned management team and technical support from JV partner – Operating since 1994, EBL has an adequate track record of operations in the Nepalese banking industry. The bank is led by an experienced management team and is supported by its JV partner Punjab National Bank (which holds ~20% shares in EBL) under a Technical Support Service Agreement (TSSA). The senior management team[3] at EBL comprise of seconded staffs from PNB under the terms of TSSA which enables the transfer of knowhow from PNB to EBL to some extent.

Controlled growth – EBL has the history of conservative growth strategy despite its good competitive positioning; partly stemming from its scrupulous underwriting norms. The bank grew both its credit and deposit by CAGR of ~12% in the last five years ending mid-July 2023 vis-à-vis the industry average growth of ~15% (credit) and ~16% (deposit) during the same period. Although this has resulted in a loss of market share in recent years, relatively seasoned credit portfolio for EBL remains a comfort against the future asset quality concerns created by uncertain and difficult economic condition to some extent. This is also reflected in strong assets quality reported by the bank in the recent years.

Comfortable assets quality and solvency profile – Despite recent deterioration, EBL's NPA of ~0.79% as of mid-July 2023 remains well below the industry average NPA. Similarly, EBL's 0+ days delinquencies of ~11% as of mid-July 2023, remains lower than many peers despite the uptick from ~7% as of mid-July 2022. EBL's solvency ratio also remains comfortable at present with net NPA to net worth ratio of ~2%. EBL's ability to attract better clientele by offering finer lending rates, its slow credit growth, relatively seasoned credit portfolio and conservative underwriting norms remain a comfort against possible slippages in future. Nonetheless, majority of the borrowers from the banking industry (including EBL) are under some form of liquidity stress in the recent period amid the tighter regulations from central bank. EBL's ability to manage its incremental asset quality, therefore, will remain a key rating monitorable.

Good capitalization and liquidity profile – EBL reported a CRAR of ~13.3% and Tier I capital of ~11.2% as of mid-July 2023, which remains comfortable vis-a-vis the regulatory minimum of 11% and 8.5% respectively. The bank has maintained an adequate capital cushion over the years, supported by its good profitability profile, controlled credit growth in recent years and controlled dividend outflow in FY2021 and FY2022. EBL has a comfortable liquidity position, with healthy liquid assets/total asset ratio stood at ~30% and regulatory CD ratio of 83% as of mid-July 2023.

Profitability supported by low operating expenses and credit cost; recent improvement in NIMs remains positive – EBL's profitability ratios reported moderation in FY2020 and FY2021 after the reduction in regulatory interest spread and has improved from FY2022 onwards. EBL's NIMs has also reported a turnaround from FY2022 which remains a positive for incremental profitability prospects, given the relatively moderate non-interest income ratio. EBL reported a better-than-industry average return on net-worth (RONW) for the first time in last three years in FY2023. In addition to the improved NIMs, EBL's profitability also remains supported by low operating expense ratio and relatively lower credit cost.

Credit challenges

Portfolio concentration – EBL's portfolio remains relatively concentrated in terms of both deposits and credit. As of mid-July 2023, concentration among top 20 borrower groups accounted for ~22% of total loan portfolio (~163% of tier I capital) while the concentration of top 20 depositors also stood at ~22% of total deposits. High credit concentration poses credit repricing risks and asset quality concerns for the bank to some extent, despite being comforted by good borrower profile.

3 *TSSA provides for a maximum of three seconded staff from PNB, one of which will be EBL's Deputy CEO.*

Similarly, high deposit concentration increases repricing risks and raises concerns over liquidity position of the bank at times of interest rate volatility.

Low non-interest income levels limits revenue diversification – EBL reported a non-interest income level of ~0.6% of total assets for FY2023 vs. 0.74% for FY2022; which remains lower than many established players in the industry. Low non-interest income level of the bank limits revenue diversification which could subdue profitability during the period of subdued NIMs.

Regulatory risk and difficult operating environment – The banking industry as well as banking sector borrowers have been facing stress from H1FY2022, following the roll-back of Covid-relaxations and introduction of stringent regulations affecting the fresh credit creation. The incremental regulatory changes have also remained stringent such as higher provisioning for group units in case of stress developed in any unit. The borrowing rates has remained sticky at higher level which has reduced the repayment ability of borrowers which coupled with the ineligibility of many borrowers for fresh loans after the implementation of working capital guidelines, could create asset quality stress and remains a rating concern across the industry.

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

Links to applicable criteria:
Bank Rating Methodology
Issuer Rating Methodology

Company profile

Operating since October 1994, Everest Bank Limited (EBL) is one of the oldest private sector banks in Nepal. EBL is a joint venture with Punjab National Bank (PNB), India which holds ~20% stake in EBL. The bank also has a Technical Service Agreement (TSA) with PNB. EBL has 70:30 promoter: public shareholding ratio. Mr. B.K. Shrestha, the current chairman, directly/indirectly holds a significant stake in the bank.

As of mid-July 2023, EBL has presence throughout the country through its 127 branches. Following recent loss of market share, EBL currently holds ~3.3% market share in banking industry deposit/credit and ~3.7% in the commercial banking deposit/credit. EBL reported a profit after tax (PAT) of ~NPR 3,393 million during FY2023 over an asset base of ~NPR 249 billion as of mid-July 2023 vs. PAT of NPR 2,479 million during FY2022 over an asset base of NPR 225 billion as of mid-July 2022. As on mid-July 2023, EBL has gross NPL of 0.79% and CRAR of 13.36% (including tier I capital of 11.23%).

Key financial indicators

YEAR ENDED	Mid-July 2020 (Audited)	Mid-July 2021 (Audited)	Mid-July 2022 (Audited)	Mid-July 2023[4] (Provisional)
Net Interest Income – NPR Million	5,310	3,956	5,181	7,448
Profit before tax – NPR Million	3,582	2,548	3,548	4,847
Profit after tax – NPR Million	2,516	1,771	2,479	3,393
Loans and advances – NPR Million	118,712	132,214	153,093	168,123
Total assets – NPR Million	185,023	211,650	225,381	249,983
OPERATING RATIOS				
Yield on average advances	10.89%	7.58%	9.25%	12.04%

4 Annualised

YEAR ENDED	Mid-July 2020 (Audited)	Mid-July 2021 (Audited)	Mid-July 2022 (Audited)	Mid-July 2023[4] (Provisional)
Cost of average deposits	6.26%	4.91%	5.85%	7.55%
Net Interest Margin/Avg. Total Assets	3.00%	1.99%	2.37%	3.13%
Non-interest Income/Avg. Total Assets	0.79%	0.68%	0.74%	0.58%
Operating Expenses/Avg. Total Assets	1.46%	1.26%	1.34%	1.36%
Credit Provisions / Avg. Total Assets	0.31%	0.13%	0.15%	0.31%
PAT / Avg. Total Assets	1.42%	0.89%	1.13%	1.43%
PAT / Net Worth	13.88%	9.01%	11.41%	14.05%
Gross NPAs	0.22%	0.12%	0.12%	0.79%
0+ days delinquencies			6.72%	11.05%
CAPITALISATION RATIOS				
Capital Adequacy Ratio	13.38%	12.48%	11.89%	13.36%
Tier I Capital	11.92%	11.24%	10.78%	11.23%
Net NPAs/Net Worth	0.63%	0.22%	0.02%	1.87%
COVERAGE & LIQUIDITY RATIOS				
Total Liquid Assets/Total Liability	33.28%	33.83%	28.25%	29.97%
Total Advances/Total Deposits	82.95%	84.37%	89.38%	84.51%

Source: *Company Data*

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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 the rating process and methodologies, analytical software, research, training, and technical and analytical skill augmentation.

Our parent company, ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment information and credit rating agency. Today, ICRA and its subsidiaries together form the ICRA Group of Companies.

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