

## Nepal Infrastructure Bank Limited: Rating reaffirmed

January 03, 2024

### Summary of rating action

Facility	Rated Amount	Rating Action
Issuer Rating	NA	[ICRANP-IR] BBB; reaffirmed

### Rating action

ICRA Nepal has reaffirmed the issuer rating of [ICRANP-IR] BBB (pronounced ICRA NP issuer rating triple B) to Nepal Infrastructure Bank Limited (NIFRA or the bank), indicating moderate degree of safety regarding timely servicing of financial obligations. Such issuers carry 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.

### Rationale

The rating reaffirmation continues to factor in the bank's strong ownership profile (including equity participation from the Government of Nepal-GoN), its experienced management team and strong capitalisation profile. Given its sizeable equity base, most of the current loan book has been funded through equity and hence the capitalisation profile is expected to remain strong over the medium term amid the generally slow disbursements towards the infrastructure projects. The competitive positioning of NIFRA remains supported by its lean organisational set-up, which enables it to offer competitive lending rates (notwithstanding the funding constraints). The rating also factors in the positive long-term demand outlook for the infrastructure financing, given the large infrastructural gap in Nepal. The need to minimise interest rate fluctuation in long-term projects by minimising the asset-liability maturity mismatch, could also offer growth scope for institutions such as NIFRA that collects long-term funds to finance such projects.

Nonetheless, the rating continues to remain constrained by the bank's limited track record, inherent risk associated with the infrastructure financing and relatively unseasoned credit book (~60% portfolio still under moratorium) and hence untested underwriting norms. The portfolio concentration also remains high given the large ticket size involved in infrastructure financing. Rating concerns further arise from the increase in portfolio delinquency (~28% as of mid-October 2023 compared to ~17% as of mid-October 2022). While the relatively relaxed non-performing loan (NPL) classification and provisioning norms for infrastructure bank provides near term comfort, NIFRA's ability to maintain its asset quality profile, once the repayment starts for large part of the portfolio, remains to be seen. Accordingly, its ability to maintain adequate capital cushion on an ongoing basis will be essential to maintain long-term solvency.

The incremental growth outlook for the bank will depend on its ability to ensure timely and adequate funding, which remains a concern amid the lukewarm subscription (~46%) of its energy bond issued in FY2023, despite eligibility for subscription by banks and financial institutions (BFIs) to meet their quota of infrastructure lending. The restriction on infrastructure banks to raise only the long-term funds through term deposits and the low subscription of the recent energy bond, indicates its option of the high-cost funding only in the domestic market. NIFRA is in accreditation process for accessing the offshore borrowings and hence timely access to these funds at competitive rates will remain crucial for its long-term viability. Overcoming the funding constraints will depend on NIFRA's ability to capitalize on the regulations and/or the ability of the management to develop traction with large-scale depositors as well. Going forward, NIFRA's ability to seek and secure the sources of funds for its long-term growth and manage the asset quality on its lending portfolio will be the key rating sensitivities.

## Key rating drivers

### Credit strengths

**Strong ownership and seasoned management team** – NIFRA has been set up in the private-public partnership (PPP) model with equity participation from the GoN, private sector investors and public. The major promoters of NIFRA include the GoN, leading players in the banking sectors, insurance sectors and individuals and institutions related to large business houses in Nepal such as the Vishal Group, the IME Group, the Lucky Group etc. As of mid-October 2023, the paid-up capital of NIFRA was distributed among class A banks (~21%), life insurance companies (~16%), the GoN (~10%), individuals and private institutions (8%) and other public companies (2.5%). This blend of general public, government, public limited companies and private sector investors remains a positive from the governance and growth aspects of NIFRA. Also, the senior management team and the department heads of NIFRA comprise seasoned players from the banking industry, which provides comfort to its management profile.

**Positive demand outlook given the need to reduce interest rate volatility in long-term project financing** – The demand for infrastructure financing in Nepal remains favourable given the gap in the current infrastructural funding needs and availability. This remains positive for the growth of NIFRA. At the same time, liquidity and interest rates in the Nepalese banking sector have remained volatile historically given the asset-liability maturity mismatch in the players' balance sheet, exposing long-term projects to the risks arising from the same. NIFRA's business model of using long-term funds to finance the long-term projects could help reduce such risks for the projects, which could further support the demand outlook for NIFRA.

**Lower operating cost adds to competitiveness** – NIFRA's organisational set-up remains lean with focus mainly on the infrastructure related project financing (such as energy, roads, hotels, hospitals, transportation, communication, primary manufacturing like Cement etc). As a result, the operating cost of the bank remains low. In the intensely competitive banking sector, this is likely to help NIFRA to operate on a low margin, thereby increasing its competitiveness vis-à-vis its banking sector counterparts. However, this will depend on its ability to raise adequate funds without elaborate network for deposit/fund collection.

**Strong capitalisation remains a comfort against probable near-term credit shocks** – As of mid-October 2023, NIFRA maintains a strong capitalisation ratio (tier-I capital of 93.48%) primarily because of relatively low-risk assets and credit exposure vis-à-vis the company's sizeable capital base. Given the staggered nature of lending and this the expected slower growth in risk assets, NIFRA is likely to maintain a low leverage and strong capitalisation over the medium term. This is likely to help it absorb any probable credit shocks over the medium term. However, maintaining adequate capital cushion on an ongoing basis will be essential for NIFRA's long-term solvency, considering the risks of the infrastructure financing segment and lumpiness of its credit portfolio.

### Credit challenges

**Relatively high delinquency level raises long-term asset quality concerns** – As of mid-October 2023, the 0+ days overdue for NIFRA remained on a higher side at ~28% (~17% as of mid-October 2023), which raises major asset quality concerns, especially considering the fact that repayment has started for only ~40% of the bank's portfolio. Although the portion of overdue instalment is low, the tendency of projects to delay its repayment subsequently after its commissioning or shortly after inbounding by NIFRA, raises concern on the underwriting quality as well as the repayment capacity until the projects reach stabilisation phase.

The bank's asset quality is also benefitted by flexible NPL recognition norms for the sector wherein 90+ days delinquencies and only the overdue portion for term loans is accounted as NPLs. Further, the reported profitability was also aided by relatively low provisioning norms for the sector. NIFRA's effort to regularise delinquencies could be challenged by the ongoing unfavourable economic conditions, general demand slowdown for industrial/service sector outputs, despite moderating interest rate outlook, which could further erode the borrowers' credit profile. Considering the majority proportion of projects under moratorium phase, the repayment capacity of the credit book is yet to be fully tested. Moreover, given the low granularity in the infrastructure sector lending, any slippages in the credit portfolio will have a bearing upon bank's future profitability and return indicators.

**Raising of long-term funds at competitive rates remains a challenge** – As per the current regulations, NIFRA is restricted to only raise long-term deposits in the domestic market alongside the bonds and other borrowings. Hence, raising requisite funds from the domestic market by competing with other BFIs with a much wider depositor base will remain a major challenge, unless supported by regulations. Although regulations allow NIFRA to access the offshore market to raise requisite funds, NIFRA's ability in this regard remains to be seen. Therefore, the ability to identify and raise the sources of funds at competitive rates, will have a major bearing on the long-term growth, liquidity, and overall financial profile of NIFRA. While the policy unlocking for issuance of infrastructure bonds and acceptability of the same for BFIs to meet their infrastructure lending quota was expected to help NIFRA raise adequate funds, its energy bond issued in FY2023 received lukewarm subscription (~46%), albeit partly impacted by its low coupon rate (7%). Hence, the bank's ability to raise timely/adequate fund at competitive rates remains to be seen. Further its accreditation for offshore borrowing and the bank's ability to access international funds at competitive rates also remains to be seen.

**Inherent risk in infrastructure financing and high concentration risks** – Infrastructure financing remains relatively risky given the long gestation period of the underlying projects, risks related to their execution (including time and cost overrun), stabilisation risks/loss-funding requirements in initial years of operations and offtake risks/high vulnerability to the general operating and business environment of the country. NIFRA has a mandate to invest only in the designated sectors related to the infrastructure, which limits the scope for portfolio diversification. In addition to limited sectoral diversification (~54% of total outstanding portfolio concentrated in energy sector projects), the portfolio is also likely to remain concentrated among few large projects given the large-ticket nature of infrastructure loans. This may lead to credit concentration risks for NIFRA, wherein failure of any large project could significantly impact its asset quality. High concentration in an inherently risky sector could lead to asset quality concerns for the company, especially given the unseasoned credit books and relatively untested underwriting track record of the bank.

**Link to the previous rating rationale:**

[Nepal Infrastructure Bank Limited - Issuer Rating Surveillance - December 2022](#)

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

**Links to the applicable criteria:**

[Bank Rating Methodology](#)

[Issuer Rating Methodology](#)

## Company Profile

Operating since March 2019, Nepal Infrastructure Bank Limited (NIFRA) is a special category financial institution licensed by the Nepal Rastra Bank (NRB, the central bank). NIFRA focuses on infrastructure financing by raising resources from domestic and international markets through equity, debt, mezzanine and sector fund structures, issuing on-shore and off-shore bonds and debenture etc.

NIFRA has been incorporated under a public-private partnership (PPP) model. As of mid-October 2023, the promoters hold 60% stake while the general public hold the rest. The major promoters are Government of Nepal (~10%), NRB-licensed private sector BFIs (~21%), life insurance companies (~16%), Nepal Reinsurance Company Limited. (~2.5%) and private institutions and individuals related to leading private business houses of Nepal such as the Vishal Group (major promoter of NIC Asia Bank), the IME Group (major promoter of Global IME Bank), the Lucky Group (related to Shivam Cement Group), etc. NIFRA's shares are listed on the Nepal Stock Exchange.

NIFRA reported a profit after tax (PAT) of NPR 1,399 million during FY2023 (YoY growth of 37%) over an asset base of NPR 27,922 million as of mid-July 2023. For Q1FY2024, NIFRA reported PAT of ~NPR 414 million over an asset base of ~NPR 28,181 million as of mid-October 2023.

## Key financial indicators

YEAR ENDED	Mid-July 2021 (Audited)	Mid-July 2022 (Audited)	Mid-July 2023 (Audited)	Mid-October 2023 <sup>1</sup> (Provisional)
Net Interest Income – NPR million	1,336	1,883	2,726	702
Profit before tax – NPR million	1,198	1,464	1,997	591
Profit after tax – NPR million	837	1,023	1,399	414
Loan and advances – NPR million	2,297	15,583	20,330	19,481
Total assets – NPR million	24,424	25,862	27,922	28,181
<b>OPERATING RATIOS</b>				
Yield on average advances	7.61%	9.09%	12.73%	12.20%
Cost of deposits	8.52%	6.37%	6.92%	8.13%
Net Interest Margin/Avg. Total Assets	6.96%	7.49%	10.14%	10.00%
Non-interest Income/Avg. Total Assets	0.05%	0.04%	0.08%	0.07%
Operating Expenses/Avg. Total Assets	0.68%	1.17%	1.38%	1.50%
Credit Provisions / Avg. Total Assets	0.09%	0.53%	1.42%	0.14%
PAT / Avg. Total Assets	4.36%	4.07%	5.20%	5.90%
PAT / Net Worth	4.65%	4.47%	5.93%	6.90%
Gross NPLs	0.00%	0.00%	0.00%	0.00%
0+ days delinquencies	NA	NA	27.72%	27.63%
<b>CAPITALISATION RATIOS</b>				
Capital Adequacy Ratio	305.55%	112.23%	93.48%	94.67%
Tier-I capital	305.25%	111.49%	92.69%	93.91%
Net NPLs/Net Worth	0.00%	0.00%	0.00%	0.00%
<b>COVERAGE &amp; LIQUIDITY RATIOS</b>				
Total Liquid Assets/Total Liability	90.28%	39.18%	27.66%	30.62%
Total Advances/Total Deposits	754.39%	3547.57%	2247.22%	2299.52%

For further details please contact:

### Analyst Contacts

**Mr. Sailesh Subedi** (Tel No. +977-1-4519910/20)

[sailesh@icranepal.com](mailto:sailesh@icranepal.com)

**Mr. Bipin Timilsina** (Tel No. +977-1-4519910/20)

[bipin@icranepal.com](mailto:bipin@icranepal.com)

### Relationship Contacts

**Ms. Barsha Shrestha** (Tel No. +977-1-4519910/20)

[barsha@icranepal.com](mailto:barsha@icranepal.com)

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<sup>1</sup> Profitability ratios of Q1FY2024 have been annualized.



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)

**ICRA Nepal Limited**

Sunrise Bizz Park, 6th Floor, Dillibazar, Kathmandu, Nepal.

**Phone:** +977-1-4519910/20

**Email:** [info@icranepal.com](mailto:info@icranepal.com)

**Web:** [www.icranepal.com](http://www.icranepal.com)

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