Standard Chartered Bank Nepal Limited: Rating reaffirmed

March 12, 2024

Summary of rating action

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

Rating action

ICRA Nepal has reaffirmed the issuer rating of **[ICRANP-IR] AAA** (pronounced ICRA NP issuer rating triple A) to Standard Chartered Bank Nepal Limited (SCBNL). The rating is considered to have the highest degree of safety regarding the timely servicing of financial obligations. Such issuers carry the lowest credit risk. The issuer rating is only an opinion on the general creditworthiness of the rated entity and not specific to any particular debt instrument.

Rationale

The rating reaffirmation factors in the bank's sustained strong capitalisation profile with capital to risk weighted assets ratio (CRAR) of ~16% and tier-I capital of ~13% as of mid-January 2024 against the regulatory minimum of 11% and 8.5%, respectively. The rating also factors in the bank's robust asset quality with reported gross non-performing loans (NPLs) of 1.60% as of mid-January 2024, which remains much lower as against the commercial banking industry average of 3.63%, despite the recent increase (NPLs were 0.72% as of mid-January 2023, when last rated). Additionally, the 0+ days delinquencies (0+ DPD) remain controlled at ~3.5% as of mid-January 2024, which provides additional comfort. SCBNL's established underwriting norms, robust risk management practices and its competitiveness in terms of the ability to offer finer lending rates continue to offer comfort against the bank's incremental asset quality outlook, despite the current economic slowdown. The rating action also continues to factor in the bank's long track record of operations (since 1987) and its strong parentage (~70% subsidiary of the Standard Chartered Group[1]) along with the group's management/oversight support. The bank's healthy deposit profile with relatively high share of low-cost deposits has resulted in the bank maintaining lowest cost of funds in the industry, which remains a major strength. The rating further continues to factor in SCBNL's competitive positioning underpinned by its global brand reputation and competitive cost of funds. Bank's adequate profitability indicators with return of assets (ROA) and return on net worth (RoNW) of 2.32% and ~11% in H1FY2024 (against the industry average of 1.09% and ~8% respectively) also remains a rating positive.

ICRA Nepal takes note of the bank's high concentration among top-20 borrower groups (~40% as of mid-January 2024; ~32% excluding the interbank credit purchase), on a relatively small sized balance sheet. High dependence upon large borrower groups has remained a concern, though comforted by relatively strong borrowers' profile, comprising mostly of industry leaders in their respective segments. ICRA Nepal also takes note of the stringent regulatory changes, volatile political environment which could impact the credit profile of the borrowers and overall banking industry's operating environment. Going forward, the bank's ability to continue maintaining comfortable capitalisation profile, control incremental slippages and maintain good asset quality indicators would remain a key monitorable.

Key rating drivers

Credit Strengths

Strong promoter group and experienced board/management; proven track record – SCBNL, is a subsidiary of the Standard Chartered Group, benefitting from strong parentage support through a technical services agreement (TSA) with SCB-UK. Group's representation on the bank's board and management team augurs well for the oversight support. Majority of SCBNL's multinational clientele base, bank with the Group globally, therefore are provided credit facilities in Nepal within their globally sanctioned limits. Further, SCB Group company has been extending intra-group guarantee to SCBNL on a need basis to support funding that were beyond its risk appetite, which reflects well on the stance of the

[1] The ultimate parent i.e. Standard Chartered PLC (assigned a baseline credit assessment of Baa1 by Moody's) holds ~70% stake through SCB-UK and Standard Chartered Grindlays Pty Ltd.

Group to facilitate the growth of the bank and provide it with the requisite support. The bank has been following the Group's systems and policies which ensure prudent underwriting norms and hence extensive customer screening. SCBNL is in operations from 1987 and hence has a proven track record in terms of market presence, strong financial indicators and presence of a seasoned management team, which remains a rating positive.

Healthy capitalisation profile – The bank's reported CRAR of 16.07% and tier-I capital of 13.26% as of mid-January 2024, remains strongest in the industry and when compared to the minimum regulatory requirement of 11% and 8.5% respectively. Incrementally, the bank is also comfortable to accommodate the regulatory additional 0.5% countercyclical buffer requirement to be maintained from mid-July 2024 onwards. Whilst the bank's capitalisation has slightly declined owing to sizeable tax payment in respect of the amount collected from follow-on offering (FPO) in the past, the capitalisation levels still remain healthy. SCBNL also has a comfortable liquidity position, with net liquid assets (NLAs) to total deposit ratio of ~39% and credit to deposit ratio of ~73% as of mid-January 2024 (against the regulatory floor and cap of 20% and 90% respectively).

Robust asset quality – Despite recent deterioration, SCBNL's NPL of 1.60% as of mid-January 2024 (0.72% as of mid-January 2023) remains well below the commercial banking industry average of 3.63%. Additionally, the bank's 0+ DPD also remains lowest amongst rated peers at ~3.5% as on the same date. The bank's robust underwriting norms have helped it in maintaining a strong asset quality, despite the industry wide stress. The bank's ability to attract better clients by offering finer interest rates, credit portfolio consolidation in recent times and relatively seasoned credit portfolio also remain the mitigants in controlling incremental slippages. Nonetheless, majority of the borrowers from the banking industry are under liquidity stress in recent periods amid the tighter working capital regulations from central bank, which could have a bearing over the bank's borrowers. While the relatively better financial/liquidity profile of the bank's majority borrowers (as reflected in higher chunk of investment grade rated entities at ~68%, in terms of loan outstanding, among the externally rated ~34% portfolio of the bank) provides comfort, SCBNL's ability to continuously manage comfortable asset quality will remain a key rating monitorable.

Superior funding profile – SCBNL's mix of low-cost current savings account (CASA), margin and call deposits remain healthy at ~65% as of mid-January 2024 (~61% as of mid-January 2023) against ~42% for the industry. Owing to the same, SCBNL's cost of deposit remains the lowest in the industry at 5.47% for H1FY2024, against 7.51% for the industry. This remains strongly supported by the sizeable portion of its deposits (~19% as of mid-January 2024) being in the form of foreign currency (FCY) deposits[2]. Further, sizeable chunk of interest free current deposits (~20%), has also aided the bank's cost of funds, while also remaining largely steady in terms of mix. The low-cost deposit structure results in superior competitive positioning for the bank, providing it with flexibility to be selective in terms of borrower profile.

Improved profitability – The bank also reported relatively healthy net interest margins (NIMs) of 4.34% for FY2023, which remained highest among rated peers, amid the proportionately higher improvement in the bank's lending yields and better investment yields. This aided the bank in reporting improved RoA of 2.52% and RoNW of ~18% in FY2023 (1.89% and ~13% in FY2022). Despite some moderation during H1FY2024, in line with the industry trends, the banks' profitability still stood comfortable vis-à-vis the industry average (RoA and RoNW of 2.32% and ~17% against the commercial banking industry average of 1.09% and ~8% respectively). The bank's profitability profile in H1FY2024 was supported by relatively lower operating and provisioning expenses, while the NIMs continued to remain superior among peers, despite the decline. Additionally, the bank's strong hold in the trade-based business augurs well for its non-interest income, which also continues to remain the strongest among rated peers. Going forward, the bank's ability to maintain adequate NIMs and manage the asset quality would have a strong bearing on its profitability.

Credit Challenges

High portfolio concentration risks – SCBNL's credit portfolio remains fairly concentrated wherein the top-20 borrower groups accounted for ~40% of the bank's total credit portfolio as of mid-January 2024 (~32% excluding the interbank credit purchase) and ~167% of the bank's tier-I capital. However, ICRA Nepal derives some comfort from the bank's good borrower profile with most of them being the market leaders in their respective segments and majority of the externally rated borrowers (~68%) being in the investment grade category. SCBNL's deposit concentration among the top-20 depositors also remained moderately high at ~26% as of mid-January 2024, which could lead to high interest rate sensitivity.

[2] *Details regarding cost of LCY and FCY deposits were not made available.*

Exposure to operational and regulatory risks related to the industry – The banking industry as well as banking sector borrowers have been reporting steady deterioration in credit profile following the roll-back of regulatory Covid related relaxations in H1FY2022, followed by import restrictions by the government for most part of 2022 in order to shore up foreign reserves and subsequent introduction of stringent regulations from the central bank (such as introduction of working capital guidelines, tighter norms on classification of loans and NPL recognition etc.). The recent regulations, especially the working capital guidelines, has reduced the eligibility of many borrowers for fresh credit and affected the pace of fresh credit creation by lender banks creating liquidity shortage across the businesses' supply chain which in turn has reduced the demand. As such, the credit profile of the borrowers is likely to further weaken over the near to medium term which could commensurately affect the asset quality of lending banks and remains a rating concern across the industry. Additionally, frequent changes in regulations also add up to the challenges.

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

Link to the last rating rationale:
Rationale-SCBNL Issuer Rating Surveillance February 2023

Bank Profile

Standard Chartered Bank Nepal Limited (SCBNL) is the second foreign joint venture in the Nepalese financial sector. The bank was incorporated in January 1987 as Nepal Grindlays Bank Limited and was subsequently renamed SCBNL in July 2001, following the acquisition of the parent, ANZ Grindlays Bank, by Standard Chartered Bank. SCBNL is a subsidiary of one of the largest international banking brands, which has diversified presence across the globe. The ultimate parent i.e. Standard Chartered PLC (SCPLC), United Kingdom, holds a 70.21% stake in the bank while the rest is held by the general public. SCBNL has a TSA with SCB-UK, which provides management support to the bank in the form of an expatriate CEO along with support in other management functions. The bank's shares are listed on the Nepal Stock Exchange and its registered and corporate office is in New Baneshwor, Kathmandu.

SCBNL has a presence across the country through 12 branches, three extension counters and 27 ATMs as of mid-January 2024. As on the same date, SCBNL had a market share of 2.22% in terms of the deposit base and 2.04% of the total advances of the commercial banking industry. The bank reported a profit after tax (PAT) of NPR 3,465 million in FY2023 (~54% Y-o-Y growth) over an asset base of NPR 151,378 million as of mid-July 2023. For H1FY2024, the bank has reported a PAT of NPR 1,726 million over an asset base of NPR 146,517 million as of mid-January 2024. As of the same date, SCBNL's CRAR stood at 16.07% and gross NPLs at 1.60%. In terms of technology platforms, SCBNL uses the global technology platforms of the Standard Chartered Group across all its branches.

Key financial indicators

Year ending on	Mid-July 2021 (Audited)	Mid-July 2022 (Audited)	Mid-July 2023 (Audited)	Mid-January 2024 (Provisional)
Net interest income - NPR million	2,594	3,740	5,956	2,631
Profit before tax - NPR million	2,008	3,232	4,960	2,466
Profit after tax - NPR million	1,399	2,256	3,465	1,726
Loan and advances - NPR million	71,892	89,745	94,516	91,830
Total assets - NPR million	114,739	123,356	151,378	146,517
Operating ratios				
Yield on average advances	6.95%	7.57%	11.59%	9.85%
Cost of deposits	2.97%	3.78%	5.83%	5.47%
Net interest margin/average total assets (ATA)	2.24%	3.14%	4.34%	3.53%
Non-interest income/ATA	1.27%	1.34%	1.38%	1.38%

Year ending on	Mid-July 2021 (Audited)	Mid-July 2022 (Audited)	Mid-July 2023 (Audited)	Mid-January 2024 (Provisional)
Operating expenses/ATA	1.43%	1.65%	1.67%	1.53%
Credit provisions/ATA	0.35%	0.11%	0.44%	0.07%
PAT/ATA	1.21%	1.89%	2.52%	2.32%
PAT/net worth	8.93%	13.13%	18.11%	17.47%
Gross NPLs	0.96%	0.59%	1.18%	1.60%
0+ days delinquencies	4.02%	1.62%	3.96%	3.52%
Capitalisation ratios				
Capital adequacy ratio	17.17%	15.95%	17.09%	16.07%
Tier-I Capital	15.53%	14.40%	14.17%	13.26%
Net NPLs/net worth	1.67%	1.11%	2.25%	3.26%
Liquidity ratios				
Total liquid assets/total liability	36.53%	25.94%	35.87%	36.40%
Total credit/ deposit	74.91%#	87.91%*	77.61*%	73.21%*

#CCD ratio as per earlier NRB guidelines **CD ratio as per current NRB guidelines*

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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.

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.

For more information, visit www.icranepal.com

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