ICRA NEPAL

Excel Development Bank Limited

ICRA Nepal assigns [ICRANP] IPO Grade 4+ to the proposed Equity Share (Rights Issue) of Excel Development Bank Limited

Facility/Instrument	Issue Size	Grading Action (November 2015)
Rights Share Issue	NPR 52.5 million	[ICRANP] IPO Grade 4+ (Assigned)

ICRA Nepal has assigned an "**[ICRANP] IPO Grade 4+**", indicating below-average fundamentals to the proposed rights issue amounting NPR 52.5 million of Excel Development Bank Limited (EDBL). ICRA Nepal assigns IPO grading on a scale of IPO Grade 1 through IPO Grade 5, with Grade 1 indicating strong fundamentals and Grade 5 indicating poor fundamentals. For the Grading categories 2, 3 and 4, the sign of + (plus) appended to the Grading symbols indicate their relative position within the Grading categories concerned. Thus, the Grading of 2+, 3+ and 4+ are one notch higher than 2, 3, and 4, respectively. EDBL is proposing to come out with 25.93% rights issue of 525,000 numbers of equity shares of face value NPR 100/- each to be issued to the existing shareholders at par. The proposed issue is being made in order to augment the capital base to support the future growth plans of the management.

The grading is constrained by buildup of delinquencies[1] in EDBL's books during the last few months[2] on account of uncertain operating environment created by ongoing political turmoil in the southern plains of the country impacting the overall economy and repayment capacity of the borrowers. This could impact the asset quality indicators going forward. The grading is also constrained by EDBL's high proportion of revolving loans to relatively weaker borrower profile (~61% as on Oct-15) along with limited seasoning of a large part of the credit book due to high growth (credit portfolio has grown by around 52% in last two years), moderate capitalization profile (CRAR[3] of 11.42% as of Jul-15) with limited ability to absorb unexpected deterioration in assets quality profile, and geographical concentration (spread across 3 districts with ~85% of business being from Jhapa District alone). The grading also takes into account EDBL's small capital base compared to revised regulatory capital framework (NPR 255 million as on Jul-15 vs NPR 500 million to be met by FY17; though remains highest among three district level peers), lack of Institutional promoters and uncertain operating environment that financial institutions in Nepal are currently facing. Nonetheless the grading factors in EDBL's adequate track record (started operations in July 2005), strong deposits profile with healthy mix of low cost CASA[4] deposits (~69% as of Jul-15 vs. ~53% for industry), competitive cost of funds (3.96% as of Jul-15) allowing bank to offer rates much competitive to peers, healthy profitability indicators (PAT/ATA[5] of 2.22% and PAT/Networth of 21.98% during FY15 supported mainly by healthy NIMs[6] of 5.44%), fair assets quality so far (Gross NPLs[7] of 1.61% as of Jul-15), moderate credit and deposit concentration (~12% and ~10% on top 20 accounts respectively), experienced management team and regulatory arbitrage available with 'Schedule B' Development Banks compared to 'Schedule A' commercial bank-in the form of lower CRR/SLR[8] requirements. ICRA Nepal also notes the limited impact of April-2015 earthquake in the area of operations of EDBL. Going forward, EDBL's ability to scale up its operations ensuring efficient utilization of additional capital, maintain its profitability profile and manage the delinquency levels would have a bearing on the overall financial profile.

[1] Delinquent loans on mid-Oct-15 accounted for ~18% of total loans vs. ~14% in mid-July-15.
[2] Mid-Oct-15 are provisional and all calculations are based on the data provided by management of GBBL
[3] Capital to risk adjusted assets ratio
[4] Current and Savings Accounts
[5] Profit after tax/Average total assets
[6] Net Interest Margins
[7] Non-Performing Loans
[8] Cash Reserve Ratio/ Statutory Liquidity Ratio

The credit portfolio of EDBL has grown at a CAGR[9] of ~19% during the past 5 years (vs. 24% growth in industry) however, the portfolio size still remains small at NPR 2,144 million as of Jul-15 (NPR 2,281 million as of Oct-15). The healthy credit growth has been supported by EDBL's adequate franchise of 13 branches; with major business concentration (~85%) in Jhapa district. The bank is able to offer lower rates to its customers backed by low cost deposit profile and hence the yield on advances remain lower among peers at ~13% as of Jul-15. The credit portfolio as on Oct-15 was mainly composed of Overdraft/ Working capital Loans (61%), Term Loans (18%), Housing loan (11%), Personal Loans (4%) among others. EDBL's credit concentration remains moderate (top 20 borrowers accounting for 11.83% of total loans on Jul-15) better compared to most of the new generation development banks.

EDBL's assets quality has remained fair so far with gross NPLs of 1.61% on Jul-15 as against 1.88% on Jul-14 (Vs. 3.58% and 4.16% for industry respectively); partly benefitted by high proportion of revolving loans where repayment capability of the borrowers remains to be tested. However, post July-15 EDBL has witnessed growing loan delinquencies with weak recovery profile on account of elongated strike in terai region. This could impact EDBL's assets quality going forward. Delinquent loans on mid-Oct-15 accounted for ~18% of total loans vs. ~14% in mid-July-15. Though the regulator has provided some temporary relaxations in NPL recognition norms recently factoring in the strike, the same is expected to defer the actual impact in asset quality towards year end, should the current scenario extend for a longer period of time. Further, portfolio vulnerability remain high vs. commercial banks due to inferior borrower profile and assessed income based product lending, which could lead to volatility in asset quality indicators. Although EDBL's portfolio was not impacted directly by the earthquake, the exposures in unaffected geographies/segments could witness some stress due to overall moderation in economic activity as well as linkage among businesses/borrowers.

As for funding profile, EDBL's cost of funds (3.96% for FY15 vs. industry average of 6.20%) remains competitive among peers; allowing the bank to offer better interest rates and also to maintain adequate profitability at the same time. EDBL has a healthy proportion of low cost CASA deposits (~69% as on Jul-15 as compared to industry average of ~53%) along with relatively lower deposit concentration (9.78% of total deposits on Jul-15 among top 20 depositors). Lower CD ratio (~65% as of Jul-15) on account of capital constraints on growth in past, provide adequate room for immediate credit growth; capitalisation levels notwithstanding. Going forward, the ability of EDBL to maintain the deposits profile will have a bearing on overall competitive positioning.

EDBL reported profit after tax (PAT) of NPR 71 million in FY15 (corresponding to return on net worth of 21.98% and return on assets of 2.22%) and NPR 60 million during FY14 (corresponding to a return on net worth of 23.49% and return on assets of 2.06%). EDBL's profit was primarily supported by healthy NIMs (NIMs were 5.44% as of Jul-15) and low provisioning expenses. Going forward, the profitability profile of the bank will depend on its ability to expand its scale of operations thereby achieving scale economies and control over its recovery profile; the same however remains a challenge given intense competition among the BFIs in the region and economic impact of elongated strike in the region.

Capitalization profile of EDBL remains moderate with CRAR 11.42% on Jul-15 as against minimum regulatory requirement of 11% for class B banks; with tier I capital of 10.68%. As the capital requirements for business growth were met only from internal capital generation over past few years, lower capital impacted EDBL's growth. The proposed rights issue along with the internal accruals would help bank maintain adequate capitalization over the medium term. However, monetary policy of FY 2015-16 has announced that development banks operating up to 3 districts are required to increase their paid-up capital to NPR 500 million within FY17. EDBL has a capital of NPR 255 million as of mid-Jul-15 (highest among

[9] Compounded annual growth rate

similar scaled banks) and same is expected to increase to NPR 308 million after proposed right issues (assuming full subscription), thus the bank is likely to meet the regulatory minimum capital from internal generations till FY17 and certain portion of fresh issue to meet the shortfall. Attaining adequate growth to ensure efficient utilization of the enhanced capital would, however, remain a key challenge for the bank.

Company Profile

Excel Development Bank Ltd (EDBL) started its commercial operations from July 2005, as a 3 district level development bank. Its Registered Office is located at Birtamode-7, Jhapa. EDBL is promoted by 34 individual promoters from diverse backgrounds, with maximum shareholding by one individual at 9% of total capital. Share capital of the company is distributed among promoter & public in the ratio of 70:30. Mr. Dinesh Kumar Pokharel is the Chief Executive Officer of the bank. The bank's equity shares are listed on the Nepal Stock Exchange.

EDBL currently operates in Jhapa, Ilam and Morang districts of Nepal through its 13 branches and 2 extension counters. EDBL has market share of about 1.25% in terms of deposit base and 1.11% in terms of credit portfolio of Development banks as on mid Jul-15. EDBL reported a net profit of NPR 71 million during 2014-15 over an asset base of NPR 3,356 million as on mid Jul-15 as against net profit of NPR 60 million during 2013-14 over an asset base of NPR 3,075 million as on mid Jul-14. EDBL's CRAR was 11.42% and gross NPLs were 1.61% as on mid-Jul-2015. In terms of technology platform, EDBL has implemented Pumori Plus IV System across all its branches.

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