

Sajha Bikas Bank Limited

ICRA Nepal assigns [ICRANP] IPO Grade 5 to the proposed Equity Shares (Rights Issue) of Sajha Bikas Bank Limited

Facility/Instrument	Issue Size	Grading Action (February 2017)
Rights Share Issue	NPR 50 Million	[ICRANP] IPO Grade 5 (Assigned)

ICRA Nepal has assigned an “[ICRANP] IPO Grade 5”, indicating poor fundamentals to the proposed rights issue amounting to NPR 50 million of Sajha Bikas Bank Limited (Sajha). 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. Sajha is proposing to come out with 1:2 rights issue of 500,000 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 to augment the capital base in line with elevated regulatory capital requirements. Assuming the full subscription of the right issue, the bank will still not meet the enhanced capital requirements stipulated by NRB which is required to be met by July 2017 and hence may constrain its future operations and growth.

The grading is primarily constrained by bank’s inferior loan underwriting norms resulting in significant stress over asset quality (NPLs¹ of ~5% and delinquencies of ~47% as of Oct-16²) and limited operating track record (since April 2013). The grading is further constrained by track record of losses due to poor asset quality and is reflected in accumulated losses (equivalent to ~25% of paid up share capital as of mid-Oct-16), high customer concentration risks (~27% of credit and ~36% of deposit among top 20 customers as of mid-Oct-16) along with weak deposits profile (~48% CASA³ deposits vs. ~55% for industry as of mid-Oct-16). ICRA Nepal also takes note that despite flexibility to operate in three districts, the bank has high geographical concentration towards Kailali district (~80% business concentrated in this district) and small scale of operations⁴. In ICRA Nepal’s view, the bank has higher portfolio vulnerability due to relatively inferior borrower profile vs. commercial banks as lending is mostly based on assessed income based appraisal, which leads to higher delinquencies resulting volatility in asset quality and profitability indicators. While assigning the grading, ICRA Nepal has also factored in Sajha’s existing capital base being much lower to revised regulatory capital framework to be complied by Jul-17 and even after completion of the proposed right issue it will not be able to meet the required capital levels. This could result in restriction upon business expansion and may also require bank to be merged with other banks. The grading also remains constrained by stiff competition with commercial banks offering products at finer rates and uncertain political and operating environment that financial institutions in Nepal are currently facing.

ICRA Nepal however considers the regulatory arbitrage available with ‘Schedule B’ Development Banks compared to ‘Schedule A’ commercial bank-in the form of lower absolute capital requirements and lower CRR/SLR⁵ requirements. Going forward, Sajha’s ability to find adequate sources to attain revised regulatory capital within stipulated time (by July 2017), scale up its operations, improve its asset quality and profitability profile significantly would have a bearing on the overall financial profile.

Bank achieved high business growth albeit on small base (credit and deposits grew by CAGR⁶ of ~98% and ~107% over last three years). Sajha’s credit portfolio of NPR 378 million as of mid-Oct-16 primarily composed of business loans (50%), agriculture loans (31%), personal loans (~7%), housing loans (5%), deprived sector loans (5%) and hire purchase loans (2%). Credit portfolio remains concentrated in Kailali

¹ Non-Performing Loans

² Mid-Oct-16 data are unaudited

³ Current and Savings Account

⁴ Asset base of ~NPR 590 million as of mid-Oct-16 as compared to ~NPR 535 million as of mid-Jul-15.

⁵ Cash Reserve Ratio/ Statutory Liquidity Ratio for Schedule B bank is 5%/9% as against 6%/12% for Schedule A banks respectively

⁶ Compounded Annual Growth Rate



district (~80%) from where it started its operations. Concentration among top 20 borrowers at ~27% as of mid-Oct-16 also remains high among peers.

Bank's asset quality witnessed significant stress over FY16 with reported Gross NPLs increasing from 1.00% as of Jul-15 to 6.12% as of Jul-16 (4.63% on Oct-16). Overall delinquencies also remain high at ~30-35% which has further moved up to ~47% as of Oct-16 despite having ~52% revolving loans where borrower has to serve interest only. Bank's portfolio vulnerability remains high vs. peers due to inferior collateral and business assessment norms resulting inferior borrower profile, malpractices⁷ followed by bank while lending to borrowers and assessed income based lending which could lead to high volatility in asset quality and profitability indicators in future as well. Owing to significant spike in NPLs and depleted equity base, impact on solvency (Net NPA/Net-worth) also remains high at 6.24% as of Oct-16. Bank's ability to downsize the delinquencies and attain requisite growth while maintaining the quality of incremental credit portfolio would have a key bearing over financial profile of the bank going forward.

As for funding profile, Sajha had ~48% low cost CASA deposits as on mid-Oct-16 vs. ~55% for industry. The cost of funds for the bank remained higher among peers (5.56% for Q1FY17 vs. 5.01% for industry) on account of inferior CASA profile. Deposits profile further remains concentrated with top 20 depositors accounting for ~36% of total deposits as of mid-Oct-16.

Sajha's profitability profile remains subdued as the bank has been reporting significant losses so far which has eroded ~25% of its net worth. The reported losses resulted in negative return on net worth of ~15% and negative PAT/ATA⁸ of 2.02% for FY16. Sustainability of the improvement in these ratios as of Q1FY17 (return on net-worth to ~28% and PAT/ATA 3.42%), supported mainly by writeback of provisions, remains a concern given the track record of significant deterioration in financial performance by year end compared to quarterly highlights. Low fee based income (1.17% of ATA for FY16) and significant credit costs (3.33% for FY16) act as a drag on profitability despite moderate NIMs (4.18% for FY16). Incrementally, Sajha's earnings profile will largely depend on the ability of the bank to improve its asset quality and hence reduce credit costs thereby improving the NIMs. Ability of Sajha to recover the accumulated losses remains to be seen.

Sajha's CRAR⁹ was 16.97% as of mid-Oct-16, higher than the regulatory minimum of 11%. Monetary policy of FY 2015-16 has announced that three district level development banks are required to increase their paid-up capital to NPR 500 million within Jul-17 failure to comply the same may constrain growth. Sajha has a capital of NPR 100 million as of mid-Oct-16 and the same is expected to increase to NPR 150 million after proposed issue (assuming full subscription). Post proposed issue, bank has to merge or be acquired by other bank in order to fulfil the elevated capital requirements; however, finding suitable partner within limited time frame remains a key challenge for the bank as inability to find sources for capital increment will result in restriction in business expansion. The bank's ability to raise shortfall capital in a timely manner would also have critical bearing on its ability to absorb any significant deterioration in asset quality and maintain comfortable solvency profile.

Company Profile

Established in August 2012, Sajha started its commercial operation as three district level development bank from April 2013. Its corporate office is located at Main Road, Ratopul, Dhangadhi. The bank was promoted by a group of individuals involved in different professions with maximum shareholding by one individual 12.55% of total capital as on Oct-2016. Share capital of the bank is distributed among promoter & public in the ratio of 51:49. The shares of the company are listed on the Nepal Stock Exchange. Mr. Chandra Bahadur Bohara is the General Manager of the bank.

Sajha has presence in 3 districts of Nepal (out of its working area of 3 districts) through its 6 branches and 2 extension counters. Sajha has market share of about 0.16% in terms of deposit base and 0.15% in terms of credit portfolio of development banks as on mid Oct-16. Sajha reported a net loss of NPR 11 million during 2015-16 over an asset base of NPR 587 million as on mid Jul-16 as against net profit of NPR 0.51

⁷ Bank has disbursed loan without approval, disbursed loan more than approved limit and advanced fresh loan to settle earlier problematic loan interchanging branch in some cases.

⁸ Average Total Assets

⁹ Capital to Risk-weighted Assets Ratio



million during 2014-15 over an asset base of NPR 535 million as on mid Jul-15. For Q1FY17, bank has reported net profit of NPR 5 million over an asset base of NPR 590 million. Sajha's CRAR was 16.97% and gross NPLs were 4.63% as on mid-Oct-2016. In terms of technology platform, Sajha has implemented "Trust Bank" in all of its branches.

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