Manaslu Bikas Bank Limited

ICRA Nepal assigns [ICRANP] IPO Grade 4+ to the proposed Equity Shares (Rights Issue) of Manaslu Bikas Bank Limited

Facility/Instrument	Issue Size	Grading Action (May 2016)
Rights Share Issue	NPR 91.76475 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 to NPR 91.76475 million of Manaslu Bikas Bank Limited (MBBL). 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. MBBL is proposing to come out with 2:1 rights issue of 917,647.5[1] 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 to meet the elevated regulatory capital requirements as well as to support the bank's growth plans.

The grading factors in MBBL's ability to grow its portfolio (CAGR 87% over past 4 years ending FY15, albeit on a small base vs. 21% for development bank industry) while maintaining healthy asset quality (0+ delinquencies ~5.5% and nil Gross NPLs[2] as on mid-Apr-15) ICRA Nepal also takes note of the improved profitability profile of MBBL while assigning the grading (RoNW of ~18% during 9MFY16 vs. 12.8% during FY15) and promoters' knowledge of its area of operations. Adequate capitalization level (CRAR[3] of 13.73% as on mid-Apr-16[4]) and expertise of management team in the local market is expected to provide MBBL with adequate growth opportunities in the near term. The grading also factors in low credit concentration among top borrowers (top 20 borrower groups accounting for ~8% of total loans outstanding as on mid-Apr-16).

The grading is however constrained by bank's limited track record (operating since Dec-2010), high geographical concentration risk (entire portfolio concentrated within three districts), small scale of operations (asset base of NPR 1,923 million as of Apr-16), and stiff competition from established BFIs/commercial banks in the region. MBBL's competitive positioning is further impacted by its cost of deposits (6.31% during 9MFY16) being higher to other development banks as well. Additionally, high concentration of deposits (top 20 depositors accounted for ~24% of total deposits on Apr-16) coupled with high CCD[5] ratio (78% on Apr-16) remains a concern from liquidity standpoint. ICRA Nepal takes note of marginal increase in delinquency level during the last few months on account of earthquake and elongated political turmoil[6] impacting the overall economy and repayment capacity of the borrowers; however, the impact of the same on incremental asset quality remains to be seen. While assigning the grading, ICRA Nepal has also factored in MBBL's paid up capital base (~NPR 184 million as of Apr-16) being significantly lower to revised regulatory capital framework to be complied by FY17 (NPR 500 million), lack of Institutional promoters, and relatively weaker borrower profile compared to commercial banks. Moreover, the grading is also constrained by uncertain operating environment that the banks in Nepal which could affect the growth of MBBL.

Nonetheless, the grading also factors in regulatory arbitrage available with 'Class B' Development Banks compared to 'Class A' commercial bank in the form of lower absolute capital requirements and lower CRR/SLR[7] requirements. Going forward, MBBL's ability to scale up its operations ensuring efficient

[1] the number will be rounded off based on final approval from Securities Board of Nepal (SEBON)
[2] Non-performing loans
[3] capital to Risk-weighted Assets Ratio
[4] mid-Apr-16 data are unaudited
[5] capital adjusted credit to deposit ratio
[6] Nepalese economy faced ~5 months long custom blockade and strikes in terai region in FY16 that ended recently.
[7] cash Reserve Ratio/ Statutory Liquidity Ratio

utilization of capital, improve its profitability profile and manage delinquencies in its portfolio would have a bearing on the overall financial profile.

MBBL commenced operations in Dec-2010 and the bank's credit portfolio stood at NPR 1,503 million as of mid-Apr-2016. The credit portfolio as on mid-Apr-16 primarily comprises personal loans (34%), housing loans (20%), gold loans (15%), business loans (12%), hire purchase loans (8%), deprived sector loans (8%) among others. MBBL's loan book is diversified with top 20 borrower groups accounting for ~8% of total loans on mid-Apr-16. Going forward, the growth plans for the bank would be dependent on MBBL managing its cost of funds and consequently offer competitive rates. While management plans to expand the franchisee network is also likely to support future credit growth; the same could be a challenge given the promoter's knowledge/ reputation limited to local market.

MBBL's operations are limited to three districts, all being impacted by April-2015 earthquake. Despite the stress in the economy due to earthquake and elongated political turmoil, MBBL has reported nil Gross NPLs on Apr-16 (vs. ~2% average for development bank industry). However, the pressure on asset quality was evident with delinquencies increasing to ~5.5% as on mid-Apr-16 from ~3.37% as on mid-Apr-15 (pre-earthquake); and the impact of same on incremental NPL level remains to be seen. Overall, MBBL's portfolio vulnerability remains high vs. commercial banks due to inferior borrower profile and assessed income based lending, which could lead to volatility in asset quality indicators.

As for funding profile, despite fair proportion of low cost CASA deposits (~56% as on Apr-16), MBBL's cost of deposits remains high. This is partly on account of sizeable long term deposits raised by MBBL at high cost in the initial years of operations (corresponding with the period of liquidity crunch in Nepalese financial sector); most of which are likely to remain with the bank till FY17 end. Higher deposit cost remains a drag to the competitive positioning of the bank, limiting the bank's ability to offer competitive rates to prospective borrowers. At the same time, MBBL's deposit remains concentrated among top deposit accounts (top 20 depositors comprise ~24% of total deposits on Apr-16). Going forward, the bank's ability to increase its depositor base thereby bringing down the deposit concentration and improve its overall cost of funds will have a bearing on overall competitive positioning in the future.

MBBL reported profit after tax (PAT) of ~NPR 24 million during FY15 (corresponding to a return on net worth of ~15% and return on assets of 1.92%). MBBL's profitability remains primarily supported by healthy NIMs[8] (5.07% in FY15, benefitted by unregulated spread rate[9]), fair level of fee based income (~1% of ATA) and low credit provisioning expenses so far. Despite the challenging backdrop during 9MFY16, bank reported PAT of ~NPR 27 million (corresponding to a return on net worth of 17.69% and return on assets of ~2.10%) primarily supported by improvement in NIMs to 5.26% backed by improvement in CCD ratio from ~71% during FY15 to ~78% during 9MFY16. The financial profile for MBBL has benefitted from low credit provisions due to healthy assets quality so far despite its operating expense ratio remaining on higher side due to small scale of business. Going forward, the profitability profile of the bank will be driven by the bank's ability to maintain its NIMs, manage its credit costs and further improve the operating scale.

MBBL's CRAR was comfortable and stood at 13.73% as of mid-Apr-16 (with tier I capital of 12.85%) as against minimum regulatory requirement of 11% for class B banks. Monetary policy of FY 2015-16 has raised the minimum paid up capital requirement for 3-district level development banks to NPR 500 million to be met within Jul-17. MBBL has a capital of ~NPR 184 million as of mid-Apr-16 and the same is expected to increase to ~NPR 276 million after proposed right issues (assuming full subscription). Finding adequate sources to meet the elevated regulatory requirement (through merger or raising fresh capital) and maintaining adequate returns over increased capital base would also remain key challenges for the bank.

[8] Net Interest Margins as a percentage of Average Total Assets (ATA)
[9] NRB has imposed a 5% cap on interest spread for Class A banks which has not been made mandatory for class B banks.

Company Profile
Manaslu Bikas Bank Limited (MBBL) started its commercial operation from December 2010, as a three district level development bank. Its Corporate Office is located at Gorkha Municipality-1 in Gorkha District. MBBL is promoted by 104 individual promoters from diverse backgrounds, with maximum individual shareholding of 8.41% (mid-Apr-16). Share capital of the company is distributed among promoter & public in the ratio of 70:30. Mr. Durga Ram Puri is the acting General Manager of the bank.

As on mid-Apr-16, MBBL has a network of 7 branches and 2 extensions counter across all 3 licensed districts. The bank has market share of about ~0.7% in terms of deposit base/credit portfolio of Development Banks as on mid-Apr-16. MBBL reported a net profit of NPR 24.63 million during 2014-15 over an asset base of NPR 1549 million (corresponding to return on net worth and return on assets of 14.97% and 1.92% respectively) as against net profit of NPR 15.17 million during 2013-14 over an asset base of NPR 1023 million as on mid Jul-14. During 9MFY16, bank has reported net profit of NPR 27.40 million over an asset base of NPR 1,923 million (corresponding to return on net worth and return on assets of 17.69% and 2.10% respectively). As on mid-Apr-2016, MBBL reported CRAR of 13.73% whereas the gross NPLs were Nil. In terms of technology platform, MBBL has implemented Pumori-IV System across its branches.

May 2016

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