

Nepal Bangladesh Bank Limited

ICRA Nepal assigns [ICRANP] LBBB- rating to subordinated debenture programme of Nepal Bangladesh Bank Limited

Facility/Instrument	Amount (NPR million)	Rating Action (July 2015)
Subordinated debenture Program	500	[ICRANP] LBBB- (Assigned)

ICRA Nepal has assigned rating of [ICRANP] LBBB- (pronounced ICRA NP L triple B minus) to subordinated debenture programme of NPR 500 million of Nepal Bangladesh Bank Limited (NBBL). Instruments with this rating category are considered to have moderate degree of safety regarding timely servicing of financial obligations. Such instruments carry moderate credit risk. For the rating categories AA through to C, the sign of + (plus)/ - (minus) appended to the rating symbols indicate their relative position within the rating categories concerned. Thus, the Rating of BBB+ is one notch higher than BBB, while BBB- is one notch lower than BBB.

The rating factors in NBBL's long track record (operating since June 1994), institutional promoter support from IFIC Bank, Bangladesh¹ (~41% equity ownership and representation on Board of Directors; all 3 promoter directors deputed by IFIC), improvement in assets quality indicators (Gross NPLs 1.35% as of Jul-14 and 1.93% as of Apr-15 vs. 18.17% as on Jul-11), modest operating profitability profile vs. peers (though overall profitability supported by income from recovery from NPLs/written off loans) and experienced management team. However, the rating is constrained by NBBL's relatively lower capitalisation level (CRAR² of 10.63% as on mid-Apr-2015), inferior deposit profile with high deposit concentration (42% among top 20 depositors as of Apr-15) and moderate CASA³ deposit proportion (37% of total deposits on mid-April-15 vs industry average of ~48%). The rating is also constrained by NBBL's moderate franchise⁴ leading to lower market share with ~1.91% share in Nepalese banking sector credit on mid-April-15 despite long track record, expected stress in the assets quality in post-earthquake scenario, unstable political conditions and uncertain operating environment that banks in Nepal are currently facing. Going forward, ICRA Nepal expects moderate level of stress on NBBL's asset quality and profitability profile over next 2-3 years due to damage caused by the earthquake in April 2015 and aftershocks. At this stage, exact quantum of damage is not ascertainable. ICRA will closely monitor the extent of damages on NBBL's financial and solvency profile, in case damages turn out to be higher, the rating could move down.

As for impact on NBBL's operations, NBBL's branches in the earthquake affected areas accounted for ~65% of the credit portfolio and ~84% of the deposits as on April-15. However, several of these businesses (end users of loans) are situated outside the earthquake affected areas due to which exact quantum of affected exposures and extent of damage could be restricted to certain sectors/segments⁵ accounting for ~1/3rd of NBBL's loan book. Apart from stress in affected geographies/segments, exposures in unaffected geographies/segments could also witness some stress due to overall moderation in economic activity as well as linkage among businesses/borrowers.

ICRA Nepal has also noted that earthquake has not caused significant stress on NBBL's deposits/liquidity profile⁶, though some withdrawals were noted in the interim period immediately post-earthquake (Deposits decreased by ~NPR 740 million in mid-May 2015 as compared to mid-April 2015 while credits saw an increase of ~ NPR 555 million during this period). However, recent activity in the stock market

¹ Rated AA2 for long term and ST2 for short term with stable outlook by Credit Rating Agency of Bangladesh

² Capital to risk assets adjusted ratio

³ Current & Savings accounts

⁴ Franchise includes 31 branches and 33 ATMs as on Apr-15.

⁵ Tourism, hydropower, real estate/construction, consumer loans, housing loans and loan book of micro finance entities

⁶ NBBL's deposits were NPR 30.33 billion on mid-June 2015 vs. NPR 29.58 billion on mid-April 2015



suggests that banks' ability to raise capital to absorb damages caused by earthquake is not significantly deterred.

As for capitalisation profile, NBBL reported CRAR of 10.63% on mid-April-15⁷ and 11.44% in July-14) vs. 10% regulatory minimum requirements. In addition to the proposed subordinated debenture issue, the bank might also need to raise additional capital over the medium term to maintain comfortable capitalisation profile given the marginal capital cushion as of now. The banks' ability to raise required capital in a timely manner would have critical bearing on its ability to absorb damages arising out of earthquake and maintain comfortable solvency profile. Further, modest operational profit levels in past and likely pressure in profit levels following the earthquake remains a challenge on internal capital generation.

NBBL's credit portfolio of NPR 25,330 million on mid-April-15 accounted for ~1.91% of Nepalese banking industry credit. NBBL's credit portfolio growth has remained high (CAGR of ~20%) in past 4 years (after being released from "Problematic" status in Jan 2010). However, the credit growth over next 1-2 years is likely to get stunted on account of lack of credit demand following recent earthquake and moderation in economic activity however reconstruction drive would support credit growth to some extent. The credit portfolio of the bank is largely concentrated towards large corporate loans (~51%), followed by Business/SME loans (~25%)⁸ and Retail loans (~24%) and. The proportion of corporate loans has declined in recent years to the benefit of Retail & SME segments which grew from 43% on July-13 to 49% on April-15. Among retail portfolio, NBBL's exposure to home and vehicle loan accounted for ~70% of retail loans. Increase in retail portfolio has also resulted in moderate concentration among top borrowers (22% of credit accounted for by top 20 borrowers on mid-Apr-15), providing some comfort.

Assets quality of NBBL has remained comfortable in past 2-3 years with Gross NPLs of 1.93% on April-15 and 1.35% in July-14, following significant accounting write-offs of loans to the tune of NPR 1,364 million during the periods from FY10 to FY12. Similarly the solvency position remained comfortable with Net NPA/Net worth of ~5% on April-15. However, asset quality is expected to come under pressure going forward due to damage caused by earthquake, impacting borrowers' ability to make repayments in a timely manner.

NBBL's Operational profitability witnessed improvement over the last 2-3 years (core operating profit/ATA improved from 2.2% as on mid-Jul-12 to 2.88% as on mid-Jul-14) with size of operations and remains modest vs. peers. Overall profitability indicators have remained good in past 3 years, largely supported by recovery from written off loans/well provided NPLs. NBBL reported PAT/ATA of ~3.76% and PAT/Net worth of ~22.42% on an average for FY12-FY14. NBBL's profitability during these years were supported by high write backs in credit provisioning expenses (average write-back of ~1.83% of ATA during FY12-FY14). In FY14 and 9MFY15, the operational profitability of NBBL was benefitted from high credit growth, healthy NIMs (~3% of ATA) and tight CCD ratio (~78% as of Apr-15) coupled with strong non-interest income (1.81% of ATA), lower credit provisioning expense (0.09% of ATA), though higher operating expense ratio (~2% of ATA) affected profitability to some extent. On an overall basis, NBBL has modest profitability as reflected in PAT/ATA of 2.04% as of Apr-15 and PAT/net worth of ~15%; excluding write back, the profitability would be PAT/ATA of 1.63% and PAT/Net worth of 11.84% for the same period. ICRA Nepal expects NBBL's profitability profile to remain under pressure over next 2-3 years due to impact of devastating earthquake in 2015.

Bank Profile

Nepal Bangladesh Bank Limited (NBBL) was incorporated in 1994 as "A" class Commercial Bank in joint venture with IFIC Bank, Bangladesh. The shares of the bank are held by promoter and public in the ratio of ~52:48. Out of the total promoter holding, ~41% of total shares are held by IFIC Bank, Bangladesh, remaining being held largely by individual promoters under NB Group. Mr. Mohammad Lutfar Rahman,

⁷ Based on unaudited financials

⁸ Corporate Loans: >20 million (funded); SME loans: < 20 million, towards a single borrower or related group of borrowers.



Representative from IFIC Bank is the Chairman of the bank. Board composition of the bank constitutes of 3 representatives (including Chairman) from IFIC Bank, three representatives from among public shareholders and 1 independent director. The shares of the Bank are listed in Nepal Stock Exchange and being actively traded in with current market capitalization of about NPR 11,652 million as on 3rd June 2015. The registered and Corporate Office of the Bank is located at Kamaladi, Kathmandu.

NBBL has presence throughout the country through its 31 branches, 7 branchless banking outlets and 33 ATMs. NBBL has market share of about 1.83% in terms of deposit base and 1.91% of total advances in Nepal as on mid-April 2015. NBBL reported a profit after tax of NPR 742.34 million during 2013-14 over an asset base of NPR 30,874 million as on Jul-14 against profit after tax of NPR 778.65 million during 2012-13 over an asset base of NPR 21,802 million as on Jul-13. As of Q3 FY 2014-15, Bank has reported a net profit of NPR 513.08 million over an asset base of NPR 36,718 million. As of mid-Apr-2015, NBBL's CRAR was 10.63% and gross NPLs were 1.93%. In the technology frontier, NBBL is using "Pumori" software for the day to day operations.

NBBL was once a problematic bank mainly due to lack of Corporate Governance among its key promoter group viz. NB Group. As the loans which were provided in various names to the promoter group went non-performing, the NPLs went to ~40% and capital fund became negative by ~24% in 2006-07. Following the same, management of the bank was taken over by NRB for corrective actions. In a bid to revive the bank, IFIC Bank agreed to increase its stake in the bank by purchasing shares from the group, proceeds from which was intended to be utilised for settlement of loans outstanding from promoter groups. Accordingly, IFIC bank purchased shares from NB group and another Bangladeshi partner Bank Asia, which had 15% stake in the bank thereby increasing its total stake from 10% to ~41%. Additionally, NBBL underwent merger in January 2011 with a much smaller class C Finance Company namely Nepal Sri Lanka Merchant Bank promoted by the same group and gradually recovered loans from promoter groups. With concomitant improvement in assets quality and capital adequacy, NRB management handed over the bank to the board on January 2010. As of now, NB group holds around 10% stake in the bank with no representation in board.

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