

Nepal Investment Bank Limited

ICRA Nepal assigns [ICRANP] IPO Grade 3+ to the proposed Further Public Offer (equity shares) of Nepal Investment Bank Limited

Facility/Instrument	Issue Size	Grading Action (December 2015)
Further Public Offer (Equity)	NPR 5,341.42 Million	[ICRANP] IPO Grade 3+ (Assigned)

ICRA Nepal has assigned an “[ICRANP] IPO Grade 3+”, indicating average fundamentals to the proposed Further Public Offer (FPO) amounting to NPR 5,341.42 million of Nepal Investment Bank Limited (hereinafter referred to as NIBL). 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. NIBL is proposing to come out with FPO of 9,069,388 numbers of equity shares of face value NPR 100/- each to be issued to the general public (8,615,919 shares) at a premium of NPR 501 per share (issue price for public NPR 601 per share) and staff (453,469 shares) at a premium of NPR 260 per share (Issue price for staff NPR 360 per share).

The grading takes into account NIBL’s established track record (operating since 1986) and adequate franchise¹ leading to healthy market share (~5% in Nepalese banking sector credit and deposits as on mid-Oct-15). Adequate capitalisation levels (CRAR of ~11.3% as on mid-Oct 15) and low credit–deposit ratio² (~70% as on mid-Oct-15) are expected to provide NIBL with adequate growth opportunities. ICRA Nepal also takes note of NIBL’s experienced management team, adequate NIMs³, healthy fee based income, and improving deposit profile (CASA of ~52% as on mid-Oct-15), while assigning the grading.

The grading is however constrained by the build-up of delinquencies⁴ in NIBL’s books during last few months (from ~11% as of mid-Jul-15 to ~22% of portfolio as of mid-Oct-15) on account of uncertain operating environment created by ongoing political turmoil in the southern plains of the country impacting the overall economy and therefore the repayment capacity of the borrowers. This is further aggravated by the bank’s sizeable exposure towards sectors⁵ (~27%), repayments from which could witness higher volatility. Impact of earthquake on projects/earnings of large borrowers resulting in restructuring of almost 2.6% of the credit book. These could impact the asset quality indicators going forward and hence the bank’s performance. The grading also remains constrained on account of customer concentration risks (top 20 comprised ~32% of credit book and ~35% of deposits as on mid-Oct-15), adequate though declining return indicators (PAT/ATA of 1.58% during Q1FY16 vs. 2.43% during FY14) due to cap on interest spreads by the regulator, and various relaxations in lower provisioning norms and NPL recognition supporting the financial performance during Q1FY16. ICRA Nepal also notes that although cost of funds for NIBL remain competitive compared to banking industry, the same remains slightly inferior to some of the other larger banks of Nepal. Going forward, NIBL’s ability to scale up its operations ensuring efficient utilization of fresh capital, maintain its profitability profile and manage the delinquency levels would have a bearing on the overall financial profile.

NIBL’s branches in the earthquake affected areas accounted for >80% of the credit portfolio as of Oct-15, however several of these businesses (end users of loans) are situated outside the earthquake affected areas. Till mid-Oct-15, bank has restructured 11 accounts representing ~2.6% of portfolio as of Oct-15 due to the impact of earthquake. Additionally, large borrowers of NIBL are industrial units which

¹ 46 branches and 83 ATMs

² Adjusted for net worth

³ Net Interest Margins as a percentage of Average Total Assets

⁴ Delinquencies up to 90 days

⁵ Tourism, microfinance, real estate, consumption and hydropower sectors

are impacted by the ongoing political turmoil and unrest strikes. Amidst this backdrop, the bank witnessed increase in delinquencies from ~6% as of mid-Apr-15 to ~11% as of mid-Jul-15, which has further increased to ~22% as of mid-Oct-15. However the NPLs⁶ have declined over past few years (Gross NPLs were 3.32% as on mid-Jul-12 to 1.07% as of mid-Oct-15). The reduction in NPLs during Q1FY16 has been supported by regulatory forbearance on NPL recognition extended by NRB. The bank's ability to sustain the improvement in asset quality in light of its exposure to sectors/segments impacted by earthquake and the expected stress in exposures in unaffected geographies/segments due to overall moderation in economic activity as well as linkage among businesses/borrowers remains to be seen.

NIBL is one of the large players in the Nepalese Banking Industry with an asset base of NPR 110 billion as of mid-Oct-15. Bank's credit portfolio of NPR 74 billion on mid-Oct-15 accounted for ~5% of Nepalese banking industry credit. Bank reported portfolio growth of ~27% during FY15 significantly higher than growth of ~11% CAGR over past 5 years (ending mid Jul-15), although lower to industry average growth of ~19%. Credit demand going forward is expected to remain healthy to support the reconstruction, although the same is subject to resolution of existing turmoil and hence a pickup in economic activity. NIBL's portfolio mix primarily comprises large corporate loans (~86%) followed by retail loans (~8%) and SME loans (~6%). Due to this, credit portfolio remains fairly concentrated with top 20 borrower groups accounting for ~32% of portfolio as on mid-Oct-15, hence aggravating the asset quality related risks. Going forward, the management intends to grow cautiously until the political scenario stabilises.

The prevailing uncertain economic environment has not caused stress on NIBL's deposits/liquidity profile so far. Deposit growth has remained moderate (~13% CAGR over past five years compared to ~19% for industry) in line with credit growth pattern. With gradual improvement over the years, low cost CASA⁷ deposits for NIBL at ~52% (mid Oct-15) remains healthy (vs.~43% as of Jul-12) as against industry average of ~50% as on Oct-15. This has resulted in competitive cost of funds for NIBL at 3.22% as of mid-Oct-15, although it remains slightly inferior to some of the other larger banks of Nepal. Furthermore, deposit concentration on top 20 depositors also remains high at ~35% as of Oct-15.

NIBL's capitalisation levels are adequate with CRAR⁸ of 11.31% and tier I capital of 9.11% as of mid-Oct-2015 against minimum regulatory requirement of 10% and 6% respectively. Given NIBL's healthy internal accruals and the proposed FPO, capitalization levels are expected to remain adequate to support NIBL's growth plans over the medium term. However, deterioration in asset quality and removal of regulatory forbearance resulting in higher provisioning could pose challenges in internal capital generation. Nonetheless, recent activity in the stock market suggests that banks' ability to raise capital is not significantly deterred. Post the proposed issue (assuming full subscription), NIBL's paid-up capital would increase to NPR 7.25 bn (against NPR 6.35 bn as of mid-Oct-15) and thus would remain comfortable in attaining capital of NPR 8 bn by FY17 as required by Monetary Policy of FY16/17. The banks' ability to raise planned capital in a timely manner would also have critical bearing on its ability to absorb damages arising out of earthquake/strikes and maintain comfortable solvency profile.

As for profitability, NIBL's earnings profile remain healthy owing to its adequate NIMs (3.13% during FY15 and 2.41% during Q1FY16), healthy fee based income (1.21% of ATA⁹ during Q1FY16), low operating expense ratio (1.19% of ATA during Q1FY16) and low provisioning on account of improving asset quality reported by the bank. However, the bank has witnessed moderation in return indicators during the past few years with return on net worth (RoNW) at ~20% during FY15 (~27% during FY13) and return on assets of 2.06% during FY15 (2.76% during FY13). The moderation has primarily been due to caps on interest spreads implemented by NRB since FY15. The RoNW and RoA further declined to ~17% and 1.58% respectively during Q1FY16, and were supported by relaxations provided by regulator in credit provisioning and NPL recognition norms. Disregarding these relaxations, the return

⁶ Non-Performing Loans

⁷ Current And Savings Accounts

⁸ Capital to Risk-weighted Assets Ratio

⁹ Average Total Assets

indicators would have been further impacted. In the aftermath of April-2015 earthquake and the ongoing strikes, ICRA Nepal expects NIBL's profitability profile to remain under pressure over next 2-3 years owing to rise in provisioning expenses following incremental slippages. NIBL's profitability could also come under pressure as competition increases amongst banks for efficient utilisation of large capital to be raised by FY17 (as required by changed regulations). Going forward, bank's ability to maintain adequate NIMs and manage asset quality would have strong bearing on its profitability profile.

Bank Profile

Nepal Investment Bank Limited (NIBL), previously Nepal Indosuez Bank Ltd., was established in 1986 as a joint venture between Nepalese and French partners. The French partner (holding 50%), Credit Agricole Indosuez, sold their stake to a group of companies comprising of bankers, professionals, industrialists and businessman of Nepal in April 2002. The name of the bank was then changed to Nepal Investment Bank Limited. Mr. Prithivi B. Pande (Chairman) controls, directly and indirectly, ~50% of the voting rights of the bank. Rastriya Beema Company Ltd. (RBCL) holds 15% stake in the bank among other insurance companies, retirement fund and investment companies. The proposed FPO would increase the stake of public shareholders to 30% and maintain 70:30 promoter: public holding ratio (against 80:20 as of now). The shares of the Bank are listed on the Nepal Stock Exchange. The registered office is in Durbarmarg, Kathmandu which is also the Head Office of the Bank.

NIBL has presence throughout the country through its 46 branches and 83 ATMs. NIBL has market share of 5.28% in terms of deposit base and 5.31% of total advances in Nepal as on mid-Oct-15. The bank reported a profit after tax of NPR 1,962 million during 2014-15 over an asset base of NPR 104,345 million as of mid Jul-15 against profit after tax (PAT) of NPR 1,940 million during 2013-14 over an asset base of NPR 86,174 million as of mid Jul-14. During Q1FY16, NIBL reported PAT of NPR 423 million over an assets base of NPR 110,385 million. As of mid Oct-2015, NIBL's CRAR was 11.31% and gross NPLs were 1.07%. In terms of technology platform, NIBL has implemented FINACLE in all of its branches.

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