

Batas Investment Company Private Limited: [ICRANP] LBB/A4+ assigned

March 29, 2019

Summary of rated instruments

Instrument	Rated Amount (NPR Million)	Rating Action
Long-term loans; Fund based (hire purchase loans)	2,067	[ICRANP] LBB (Assigned)
Short-term loans; Fund based (overdraft)	12	[ICRANP] A4+ (Assigned)
Total	2,079	

Rating action

ICRA Nepal has assigned a long-term rating of [ICRANP] LBB (pronounced ICRA NP L double B) to the existing and proposed long-term loans of Batas Investment Company Private Limited (BICPL). ICRA Nepal has also assigned a short-term rating of [ICRANP] A4+ (pronounced ICRA NP A four plus) to the short-term loans of BICPL.

Rationale

The assigned ratings are constrained by BICPL's subdued asset quality indicators with high delinquencies (90+ dpd of ~10% as on mid-July 2018) given the relatively modest borrower profile compared to the borrowers in the banking sector. ICRA Nepal also takes note of the recent reduction in spreads for hire purchase financing intermediaries like BICPL to 3% from 3.5%. This is likely to impact the company's profitability profile, given its small scale of operations and competitive pressure from banks. Challenges in growth for BICPL are also a rating concern, given the tight liquidity conditions which have led to higher interest rates and muted portfolio growth of BICPL in FY2018 and H1 FY2019. The company's evolving risk management practices along with the limited geographical diversification and high operating expenses constrain the ratings. The ratings also consider the company's moderate capitalisation with gearing of ~6x as of mid-January 2019 against the regulatory cap of 10x. ICRA Nepal expects the company's gearing to remain at similar levels, given the recently increased capital requirements for the sector.

Nonetheless, the rating assignment factors in the company's long track record (operating since 2003) along with its experienced promoter profile and management team. BICPL is one of the Group entities of the established Batas Group, which has a long presence (>20 years) in the Nepalese automobile sector. Thus, BICPL can leverage on its group experience and presence in the auto sector for its business expansion. ICRA Nepal also expects timely support from the Batas Group for meeting the regulatory capital requirements and for supporting growth, if required. Going forward, BICPL's ability to attain adequate portfolio growth amid the challenges and hence attain economies of scale as well as its ability to improve the delinquencies and earnings profile will remain the key rating sensitivities.

Key rating drivers

Credit strengths

Long track record and experienced promoter/management profile – BICPL has been operating since 2003 with an increased market presence after the Nepal Rastra Bank (NRB) started regulating the sector from 2013. The company is one of the Group units of the reputed Batas Group, which has a long-standing presence (>20 years) in the Nepalese automobile sector. Association with the Group provides BICPL with financial flexibility, to a certain extent, as well as support in business growth with ~50% of its portfolio coming from vehicles dealt by its sister concerns. The promoters and management have adequate experience in the sector, which is a positive.

Diversified portfolio mix, with low share of used vehicles – BICPL's portfolio is diversified across multiple brands with ~50% of portfolio coming from vehicles financed by sister concerns. The company finances both new and old private and commercial vehicles across multiple brands. Nonetheless, it has cautiously maintained a low share of used vehicles in its

portfolio mix (~16% as of mid-July 2018), considering the riskiness of the target segment. At the same time, the portfolio is dominated by the income generating commercial vehicle segment (~75%), mostly comprising individual entrepreneurs. However, revenues may witness volatility as the income of the underlying vehicles is vulnerable to adverse economic cycles.

Credit challenges

Weak asset quality profile – Given the higher interest rate compared to banks, the profile of the borrowers approaching entities like BICPL for their financing needs, would be relatively inferior. This is reflected in the company’s asset quality profile, whereby almost all the loans were overdue as on mid-July 2018 and 90+ dpd was high at ~10% as on that date. The provisioning norms for the sector are also relaxed compared to banking, with non-performing assets (NPA) classification and provisions required only for loans which are six months past due. The proportion of such loans has also increased sharply for the company to 4.74% as of mid-January 2019 from 2.42% as of mid-July 2018, and hence remains a major rating concern. Ability to control incremental slippages and undertaking effective recoveries would remain a key monitorable.

Muted growth in recent periods and small scale of operations – After witnessing significantly high portfolio growth in FY2016, when the portfolio almost tripled, the growth has moderated with muted/low growth in H1 FY2019 (~8%, 1% decline in FY2018). This can be attributed to the gradual tightening of liquidity across the banking sector leading to rising borrowing costs and, hence deterring prospective borrowers. Growth challenges are further added by the rising number of bank branches (~50% increase in the last two years). The resultant increase in financial access has impacted the competitive position of companies like BICPL. The company has limited franchise presence with two branches presently, which also impacts its scalability.

Moderate capitalisation – As of mid-January 2019, the company had a gearing of ~6x against the regulatory cap of 10x. The regulations have recently increased the capital requirements of hire purchase financing intermediaries like BICPL to NPR 200 million to be met by mid-July 2020 and further to NPR 300 million by mid-July 2021. Against this requirement, the company had capital of NPR 178 million as of mid-January 2019. Given the challenges in growth and modest internal generation, BICPL would require external capital infusion to meet regulatory requirement and for its business expansion. ICRA Nepal expects timely support from the group, if required and envisages BICPL’s gearing to remain at similar levels over the medium term as incremental growth is expected to be modest.

Reduced spreads and rising credit costs likely to pressurise profitability – In November 2018, the NRB reduced the lending spreads for companies like BICPL to 3% from 3.5%. This, along with increasing cost of funds, intense competitive pressures and weakened asset quality, has resulted in a sharp reduction net profitability¹ (0.19% for H1 FY2019 against 1.86% for FY2018). BICPL’s net interest margins declined to 2.39% in H1 FY2019 from 4.11% in FY2018, while its credit cost increased to 1.36% from 0.36% during the above period. The operating expenses ratio however remained largely stable at about 2.1%. Going forward, the company’s ability to improve its asset quality and operating efficiencies would be crucial for incremental profitability.

Evolving risk management practices – Most of the loans were sanctioned without credit bureau checks and the lending so far is mostly based on the evaluation of the assessed income. While the revised regulations now require BICPL to obtain membership of Credit Information Bureau, ICRA Nepal notes that the risk management framework is moderate in relation to the business risk profile and could be further strengthened in the areas including credit assessment and monitoring.

Analytical approach: For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below.

Links to applicable criteria:

[Corporate Credit Rating Methodology](#)

¹ Profit after tax/average total assets (PAT/ATA)

[Bank Rating Methodology](#)

About the company

Batas Investment Company Private Limited (BICPL) is a hire purchase financing company which operates in line with broad guidelines of the Nepal Rastra Bank. It is part of the Batas Group which has long presence in Nepalese automobile sector. The company was established in 2003 by three brothers namely, Mr. Ananda Raj Batas, Mr. Shanta Raj Batas and Mr. Bipendra Raj Batas. As of now, these three promoters have an equal share in the company and are also its directors. BICPL currently operates through its head office in Pokhara and a branch office in Kathmandu.

Key financial indicators

	FY2016 (Audited)	FY2017 (Audited)	FY2018 (Audited)	H1FY2019 (Provisional)
Total income (NPR million)	94	179	247	116
Net profit (NPR million)	11	19	30	2
Net worth (NPR million)	126	179	208	230
Total managed portfolio (NPR million)	1,147	1,560	1,554	1,617
Total managed assets (NPR million)	1,179	1,609	1,616	1,662
Return on average managed assets	1.31%	1.34%	1.86%	0.19%
Gross NPA ²	2.32%	1.10%	2.42%	4.74%
Net NPA	2.32%	0.99%	1.94%	3.61%
Net NPA/Net worth	21%	9%	14%	25%
Managed gearing (times)	8.22	7.69	6.57	6.01

Source: Company data

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About ICRA Nepal Limited:

ICRA Nepal Limited, the first credit rating agency of Nepal, is a subsidiary of ICRA Limited (ICRA) of India. It was licenced by the Securities Board of Nepal (SEBON) on October 3, 2012. ICRA Nepal is supported by ICRA Limited through a technical support services agreement, which envisages ICRA helping ICRA Nepal in areas such as rating process and methodologies, analytical software, research, training, and technical and analytical skill augmentation.

Our parent company, ICRA Limited, was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment information and credit rating agency.

² Entities like BICPL are not required to report NPAs and they only create provisions for overdues more than six months; these NPA numbers are the principal outstanding on such overdue accounts.



Today, ICRA and its subsidiaries together form the ICRA Group of Companies. The international credit rating agency, Moody's Investors Service, is ICRA's largest shareholder.

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