

Sanima Bank Limited

ICRA Nepal assigns [ICRANP] LA- rating to proposed subordinated debenture of Sanima Bank; reaffirms [ICRANP-IR] A- rating to Sanima Bank and [ICRANP] LA- rating to existing subordinated debenture

Facility/Instrument	Amount	Rating Action (June 2018)
Subordinated Debenture Program	NPR 2,000 million	[ICRANP] LA- (assigned)
Issuer Rating	NA	[ICRANP-IR] A- (reaffirmed)
Subordinated Debenture Program	NPR 370 Million ¹	[ICRANP] LA- (reaffirmed)

ICRA Nepal has assigned **[ICRANP] LA-** (pronounced ICRA NP L A minus) to the proposed subordinated debenture of NPR 2,000² million of Sanima Bank Limited (Sanima). ICRA Nepal also reaffirms the rating of [ICRANP] LA- to subordinated debenture of NPR 370³ million of Sanima. Instruments with this rating are considered to have adequate degree of safety regarding timely servicing of financial obligations. Instruments with this rating are considered to have adequate degree of safety regarding timely servicing of financial obligations. Such instruments carry low credit risk.

ICRA Nepal also reaffirms the rating of [ICRANP-IR] A- (pronounced ICRA NP Issuer Rating A minus) assigned to Sanima. [ICRANP-IR] A- rating is considered adequate-credit-quality rating assigned by ICRA Nepal. The rated entity carries average credit risk. The rating is only an opinion on the general creditworthiness of the rated entity and not specific to any particular debt instrument.

The rating assigned/ reaffirmed factors in the bank's steady performance along with healthy financial and assets quality indicators on growing scale of operation. The rating also factors in fair funding mix, low portfolio concentration among top accounts and healthy capitalisation profile of the bank. The rating continues to draw support from established underwriting norms and risk management framework being practiced within the bank; as reflected in low NPA and delinquency levels. The rating action also factors in the improvement in Sanima's market positioning in recent years as a result of high portfolio growth, partly aided by expansion in its branch network. Despite its short track record as a class A commercial bank, Sanima has grown in scale at a healthy pace and remains comparable to the banks with relatively longer history. Incremental growth prospect remains supported by growing footprint of the bank, comfortable capitalization and experienced management team. Assigned rating also factors in good profitability indicators supported by steady NIMs and adequate non-interest income levels.

The ratings are however constrained by Sanima's short track record as a class A commercial bank and commensurate low seasoning of the bank's portfolio. The bank has undergone a long spell of credit growth between FY2012 and FY2017 (credit growth of CAGR 40%, albeit on a low base). Bank has added sizeable credit portfolio during the period of comfortable to excess liquidity between FY2013-FY2016; which could come under stress with rising lending rates regime. This is likely to test the quality of assets of the bank. Similarly, the deposit base of Sanima also remains unseasoned which exposes the cost of fund to sharp fluctuations with the interest rate volatility in the industry. Sanima's cost of fund remains higher to industry average and large peers despite above industry average current and savings account (CASA) deposit proportion. This could affect competitive positioning, especially in the "base rate plus" lending rate regime implemented by Nepal Rastra Bank (NRB). However, strong retail credit book of the bank results in lower repricing risk enabling the bank to pass on the increased cost to the borrowers, shielding the impact of rising cost of fund on the bank's net interest margins (NIMs) and profitability. The rating is also constrained by uncertain operating environment that the banks in Nepal are currently facing.

¹ Initially proposed as NPR 700 million. Size was reduced after NRB mandated banks to raise their equity capital by four-fold through monetary policy for FY16; making tier II instrument redundant.

² 9% Sanima Debenture 2085

³ 7% Sanima Debenture 2079

Sanima's credit portfolio has grown organically⁴ at a high pace of CAGR ~40% during FY2012-FY2017, albeit on a low base. During 9mFY2018, bank reported ~34% annualized credit growth despite the challenges in credit expansion posed by shortage of lendable deposits in the banking channels. Sanima's credit growth continues to remain driven by retail and SME segment and therefore the concentration among top borrowers (18% of credit among top 20 borrower groups in mid-April 2018⁵) has not increased despite high growth in recent years. As on mid-April 2018, Sanima's credit portfolio primarily comprises of retail loans (43%), SME/Business loans⁶ (22%), corporate loans (22%), project financing loans (8%) and deprived sector loan (4%). Incremental credit growth is likely to remain supported by Sanima's tier II bond raising program. However, given the optimum CCD⁷ ratio at present (~78% as on mid-April 2018) and shortage of lendable deposits in the banking system, future credit growth will be determined by the bank's ability to raise fresh deposits. Sanima has reported superior assets quality with gross Non-performing loans (NPLs) of 0.17% as on mid-April 2018 along with low delinquency level (~2% as on mid-April 2018). Although bank's ability to maintain good assets quality level remains a comfort, the assets quality is likely to be tested over next 12-18 months by the prevailing high interest rates.

CASA proportion of Sanima has increased to 45% during 9mFY18 after falling from 47% in FY16 to 41% in FY17. CASA proportion softened in FY17 as banks focussed on term deposits to counter the deposit crunch situation and stabilize the funding profile (term deposits grew from 27% to 42% between FY16 and FY17). Given high rate of growth in past 4-5 years, deposit books of Sanima also remains relatively unseasoned. As a result, cost of fund remains prone to the volatility of interest rate in the industry (cost of deposits doubled from 3.60% during FY16 to 7.33% during FY18). Cost of deposits of Sanima has remained ~100-125 bps higher than commercial bank average during past 1-2 years, despite the CASA proportion being at par with commercial bank average. Nonetheless, Sanima's CASA proportion remains better than most of the new age private sector players. Moreover, strong retail deposit proportion (>65% as on mid-April 2018) and management's focussed approach towards boosting savings deposits augurs well for long term stability of funding profile and cost of fund. CCD ratio of Sanima bank remains at optimum level as on mid-April 2018 (~78% vs. regulatory ceiling of 80%). Therefore, incremental credit growth is likely to remain driven by the bank's ability to raise incremental deposits. Stability of deposit is comforted by fair proportion of retail deposits and relatively lower deposit concentration among top accounts.

Sanima has reported steady profit levels during past 2-3 years as reflected in return on assets (ROA) of ~2.1% in past ~3 years (FY16-9mFY18). Profit remains supported by steady net interest margin (NIMs) of ~3.5% of Average total assets (ATA) in the interim and non-interest income level of ~1.2% of ATA. Scale economies from high growth in past years has led to decline in operating expense level which coupled with low credit cost of the bank; has supported the profitability profile. However, Sanima's average return on net worth (RoNW) as diluted in past 2-3 years due to sizeable fresh equity injection made in FY17 (through rights issue). The bank reported RoNW of ~17% in 9mFY18 vs. ~19% in FY17 and ~23% in FY16. Nonetheless, RoNW of Sanima remains comparable to industry average despite dilution. Going forward, bank's profitability will depend on its ability to achieve targeted growth by managing required funds. Profitability over next 1-2 years will also depend on the ability of the bank to maintain the assets quality on current and incremental credit portfolio.

Sanima has operated with healthy capital cushion over the regulatory minimum since its upgradation into a class A commercial bank in 2012. The bank's capital to risk assets ratio (CRAR) stood at 13.15%, as on mid-April 2018; comfortable vis-à-vis regulatory minimum of 11% under prevailing Basel III norm. Capitalization remains benefited by sizeable equity addition made in FY17 and is likely to get further boost after proposed tier II debenture raising program, assuming full subscription. Sanima's tier I capital (11.78% as on mid-April 2018) remains well above 8% to be maintained by mid-July 2018 and 8.50% to

⁴ Although Sanima acquired a 1-district level Development bank in the interim, the portfolio addition was negligible.

⁵ Data of mid-Apr-18 are unaudited

⁶ SME credit covers loan upto NPR 100 million; beyond that is corporate loans as per Sanima's internal classification.

⁷ Credit to deposit ratio adjusted for capital.

be maintained by mid-July 2019 under the Basel III norms prescribed by NRB. Therefore, capitalization levels are expected to remain adequate to support Sanima's growth plans over the medium term.

Bank Profile

Sanima Bank Limited (Sanima) started its commercial operation from 2004 as national level development bank (Class B) and was upgraded into class A commercial bank in February 2012. Its head office is located at Naxal, Kathmandu. The bank is promoted by Non-Resident Nepalese (NRN) businessman loosely affiliated under brand name Sanima Group. Major promoters of the bank included Mr. Arun Kumar Ojha (~8% shareholding), Mr. Tekraj Niroula (~8%), Dr. Niraj Govinda Shrestha (~6%), Mr. Jibanath Lamichhane (~6%), Mr. Binay Kumar Shrestha (~5%), etc. Mr. Bhuvan Kumar Dahal is the Chief Executive Officer of the bank. The bank's equity share is listed in Nepal stock exchange.

As on mid-April 2018, Sanima has presence throughout the country through its 58 branches (including head office) and 66 ATMs spread throughout the country. Sanima has market share of about 2.70% in terms of deposit base and 2.74% of total advances of Nepalese Banking Industry as on mid-Jan 2018 (3.09% and 3.15% share among the commercial banks). Sanima reported profit after tax of NPR 1,304 million during FY2017 over an asset base of NPR 69,996 million as of mid-July 2017 vis-à-vis NPR 996 million during FY 2016 over an asset base of NPR 55,965 million as at mid-July 2016. During 9mFY2018, the bank has reported a net profit of NPR 1,205 million. As of mid-April 2018, Sanima's CRAR stood at 13.15% (tier I CRAR 11.78%) and gross NPLs at 0.17%.

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For further details please contact:

Analyst Contacts:

Mr. Kishor Prasad Bimali, (Tel No. +977-1-4419910/20)

kishor@icranepal.com

Mr. Sailesh Subedi, (Tel No. +977-1-4419910/20)

sailesh@icranepal.com

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