

Siddhartha Bank Limited

ICRA Nepal assigns [ICRANP-IR] BBB rating to Siddhartha Bank Limited

	Amount (NRs million)	Rating Action
Issuer Rating	NA	[ICRANP-IR] BBB (Assigned)

ICRA Nepal has assigned rating of [ICRANP-IR] BBB (pronounced ICRA NP Issuer Rating triple B) to Siddhartha Bank Limited (hereinafter referred to as SBL). Instruments with [ICRANP-IR] BBB Rating are considered as moderate-credit-quality Rating assigned by ICRA Nepal. The rated entity carries higher than 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 of SBL factors in the bank's good market positioning in Nepal, experienced senior management, adequate capitalisation level (CRAR of 11.48% as on mid-Jan-14), adequate earnings profile (PAT/ATA of 1.61% during FY13 and 1.38% during H1FY14) and adequate network in terms of geographical presence. These positives are however offset to an extent by deterioration in asset quality profile over last two-three years (Gross NPLs rose to 3.58% as on mid-Jan-14 from 1.53% as on mid-Jul-12), higher exposure to real estate segment (around 15% as on mid-Jan-14), inferior deposit profile than industry average (CASA deposit of around 33% as on Jan-14) and absence of strong institutional promoter support. The rating is also constrained by unstable political conditions and uncertain operating environment that banks in Nepal are currently facing.

SBL has followed cautious approach during last three years in the light of growing NPLs and limited growth opportunities in the market and as a result its credit portfolio growth has been moderate with CAGR¹ of 10% over last three years which is lower than Nepal's banking industry average (CAGR around 14% over last three years). The management does not have any aggressive growth plans over the short term amidst uncertain operating environment & limited growth opportunities. Although SBL Bank is predominantly focussed on corporate loans (around 75% of total book as on mid-Jan-14), the bank is progressively diversifying its product mix in favour of Retail and SME loans (retail & SME loan increased to around 25% of total credit portfolio as on mid-Jan-14 from 20% as on mid-Jul-11). Going forward management intends to increase loan in infrastructure & hydropower sector along with SME & Retail loan.

SBL's credit portfolio is dominated by large ticket size corporate loans which accounted for over 75% of total loans as on January 2014. As on January 2014, the portfolio was diversified across loans to manufacturing sector (around 21% of the credit portfolio), trading sector (19%), real estate sector (15%), construction sector (8%) and others. SBL's exposure to the real estate sector stood higher than Nepalese Commercial Banking Industry average of 7% as on January 2014, higher exposure to real estate sector has been the key reason for deteriorating assets quality indicator over last two years (with 54% of total NPA as on Jul-13). SBL's asset quality profile witnessed constant deterioration over the last two-three years with Gross NPL increasing from 0.8% in Jul-11 to 3.58% in Jan-14. Currently, management focus is on recovery of the NPA and also intends to reduce the proportion of real estate book in total credit book. Going forward SBL's ability to maintain asset quality indicators would be a key monitorable.

SBL's capitalisation level is adequate with CRAR of 11.48% (supported by 3.13% tier II capital) as of mid-Jan-2014 against minimum regulatory requirement of 10%². However, lower level of tier I capital (8.3% as on January 2014) vis-a-vis peers, deteriorating assets quality indicators and lower internal capital generation despite healthy profitability would require the bank to raise fresh capital over medium-

¹ Compounded Annual Growth Rate

² Minimum regulatory CRAR required for dividend payment is 11%



long term to maintain adequate capitalisation. However over short term, there is headroom to raise additional tier II capital, remaining within the regulatory limits³, to support the modest growth plans of the management. As per ICRA Nepal estimates, current level of capital will support the modest growth plans of management (CAGR 12%) over medium term (next 3 years); maintaining overall capitalization in the range of around 11% with solvency indicators range bound at 11-14%, if the bank is able to maintain the NPLs at present level. In the long run, the ability of SBL to raise additional capital from its existing/ external investors will have a strong bearing on SBL's growth prospects and overall capitalization profile. SBL has been distributing significant portion of its profits (around 45% of profit over last four years) to the shareholders, affecting the rate of internal accruals.

SBL has adequate earning profile as reflected in PAT/ATA of 1-2-1.6% and return on net worth of 16-20% during last 2-3 years. The profitability is supported by healthy NIMs (around 3.5% over past 2-3 years), primarily a result of lower cost of deposits (less than 6% as on January 2014), and adequate non-interest income (around 1.7% in H1 2013-14). However part of the benefit is diluted by relatively higher operating expenses (around 2% of ATA). Going forward, bank's ability to maintain its NIMs in a competitive landscape and maintaining asset quality profile would be critical for earnings profile.

The shareholding of the bank is divided among promoters and general public; with current Promoter: Public shareholding ratio standing at 51:49. SBL has an 8 members Board of Director (4 representing promoter groups, 3 from among public shareholders and 1 independent director) & top level management with significant experience across Banking & Financial Institutions. SBL has outsourced a part of its internal audit function with provision of quarterly audits; while the remaining part is looked after by bank's in-house internal audit team.

Bank Profile

Siddhartha Bank Limited (SBL), 18th Class A Commercial Bank to be licensed by NRB, started its operation in December 2002. Shareholding pattern of the Bank constitutes of the promoters holding 51% of the shares while 49% is held by the public shareholders. Among the promoter's holding, 6% shares are held by institutional promoters and 45% by individual promoters.

SBL has presence throughout the country through its 43 branches, 2 Extension Counters, 50 branchless banking counters & 55 ATMs. SBL has market share of about 2.44% in terms of deposit base and 2.32% of total advances in Nepal as on January 2014. SBL reported a profit after tax of NPR 243 million during H1 2013-14 over an asset base of NPR 36,891 million as on Jan-14 against profit after tax of NPR 508 million during 2012-13 over an asset base of NPR 33,653 million as on Jul-13. As of mid-Jan-2014, SBL's CRAR was 11.48% and gross NPLs were 3.58%. In the technology frontier, SBL is using Flex-Cube banking software for the day to day operations which is linked to a Management Information System. A disaster recovery system (DRS) of the Bank has also been established in Bhairawa, Rupendhai.

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³ Tier II capital cannot exceed 50% of core capital, as per NRB directives. As on January 2014, SBL's tier II bond of NPR 931 million accounts for around 35% of its core capital.



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