

PRESS RELEASE

NIC ASIA BANK LIMITED

April 2023

Rating

Instrument	Amount (NPR. Mn)	Ratings	Rating Action
Issuer Rating	NA	IRN A- (Is)	Assigned

Infomerics Credit Rating Nepal Limited (Infomerics Nepal) has assigned the issuer rating of IRN A- (Is) [Single A Minus (Issuer)]. Issuer with this rating are considered to have the adequate degree of safety regarding timely servicing of financial obligations. Such issuers carry low credit risk.

Detailed Rationale

The issuer rating assigned to NIC Asia Bank Limited (NICA) derive strength from its long history of operation, coupled with its diverse geographical coverage and highly experienced promoters and management team. Further, the rating also factors stable business growth with comfortable capitalization levels, improved CASA¹ level, good profitability and diversified sector wise credit portfolio. These rating strengths are partially offset by increased delinquency and Non-Performing Loan (NPL) amid unfavorable economic environment, modest liquidity profile and intense competition. Going forward, NICA's ability to manage the incremental slippage from its delinquent credit portfolio, improve asset quality, and maintain a stable liquidity profile will be critical for its profitability and capitalization profile. This factor remains a key rating sensitivity for the bank.

Detailed Description of Key Rating Drivers

Key Rating Strengths

Long history of operation, coupled with its diverse geographical coverage and highly experienced promoters and management team.

NICA was established in 1997 and has since become a prominent player in Nepal's banking sector, with a strong presence across the country. As of January 14, 2023, the bank operates 359 branches, 105 extension counters, 81 branchless banking services, and 473 ATMs, covering all provinces in Nepal. The bank's strengths stem from its experienced and well-established promoters who have diverse backgrounds in banking, insurance, manufacturing, and international trade. The board of directors comprises distinguished businessmen and industrialists with wide-ranging expertise in financial services. The Chairman of the bank, Mr. Tulsi Ram Agrawal, brings more than five decades of experience in import-export, banking, and business sectors. The bank is led by CEO Mr. Roshan Kumar Neupane, who has been with NICA Bank since March 2008, holding various managerial positions. The senior management team, under his leadership, is equally experienced and capable.

Stable business growth with diversified investment portfolio

NICA deposits grew by 9.19% as on mid-April 2023 over FY22 end with increase in concentration of top 20 depositors from 19.61% as on mid-July 2022 to 20.99% of total deposits as on mid-April 2023. Similarly, loan and advances grew by 4.27% as on mid-April 2023 over FY22 end and stood at NPR 283,219 Mn. Compound Annual Growth Rate (CAGR) of deposits and loan & advances stands at 19% and 17% respectively as of mid-April 2023, over the same period in 2020. Further, the bank's credit policy remains strong, as

¹ Current Account Saving Account

demonstrated by the historical low levels of Gross NPLs. NICA has diversified its investment in treasury bills/bonds of Nepal Government and Nepal Rastra Bank, energy bond and equity securities of domestic corporate entities including investments towards subsidiaries.

Comfortable capitalization levels

At the end of mid-April 2023, NICA had a paid-up capital of NPR 11,564 Mn, with a Core Equity Tier I (CET-I) of 8.85% and an overall capital adequacy ratio (CAR) of 12.64%, which is above the regulatory requirement of 11% set by NRB in line with Basel III norms. However, the Tier II capital decreased to 3.79% at the end of mid-April 2023 from 4.58% at the end of FY22 as the subordinated debt approached its maturity date, leading to a decrease in overall CAR. It is crucial to monitor the bank's capitalisation position, given the potential impact on asset quality, the stretched solvency profile, and the probable introduction of a countercyclical capital buffer from FY2023-24 onwards.

Improved CASA proportion

As of mid-July 2022, NICA maintained a CASA at 40.27%, which was higher than the commercial bank industry average CASA of 37.74%. The bank also showed improvement in its CASA from 39.49% as of mid-July 2021, although it was lower than the industry average of 45.23% that year. However, as of mid-Jan 2023, NICA's CASA decreased to 38.59%. By the end of mid-April 2023, it had increased to 39.48% which remained higher than the industry average CASA. The cost of funds had increased year on year due to inflation and the current economic downturn. However, with the recent improvement in market performance, interest rates in the market have responded positively, resulting in NICA's improvement in the base rate from mid-Feb 2023. The base rate decreased to 10.71% from 11.02% as of mid-Jan 2023 and further decreased to 10.48% as of mid-Apr 2023. The bank's ability to maintain a low cost of fund in the base rate plus lending model will be crucial for its competitive positioning and sustained profitability.

Good profitability and sustained growth in total income and net profit

During FY22, NICA witnessed a significant increase of 38% in its total income, reaching NPR 35,709 Mn. This increase was fueled by growth in both interest and non-interest incomes by 39.09% and 24.98%, respectively, resulting from an improvement in the yield on advances. However, the cost of funds increased to 7.39% due to market liquidity stress, and the bank's operating expenses increased by 31.08% YoY to NPR 6,987 Mn during FY22. Despite these challenges, NICA's profitability improved, as its PAT grew by 29.33% to NPR 4,215 compared to FY21, with an improved RoTA of 1.20% during FY22 from 1.09% in FY21. In 9MFY23, NICA's total income grew by 22.07% YoY to NPR 31,275 Mn, driven by growth in interest income by 22.16% and non-interest income by 21.04%. Although interest expenses rose by 27.86% YoY during 9MFY23, the bank still managed to report an 11.61% YoY growth in its net interest income to NPR 9,217 Mn during 9MFY23. The bank's ability to continue growing its income despite rising expenses remain a positive from a rating perspective. This was reflected in a YoY PAT growth of 11.38% to NPR 4,015 Mn during 9MFY23, which was the third highest² in the industry. However, the regulatory directive to reduce interest spreads to 4% by mid-July 2023 from 4.4% may create some pressure on profitability, which the bank will need to address in order to continue its growth trajectory.

Diversified credit portfolio

NICA has a diversified credit portfolio with lending distributed across various sectors. The consumption loan segment accounts for the highest exposure of 34.23%, followed by 23.16% towards the wholesaler & retailer segment, 14.41% towards others and 10.40% towards agriculture & forest related segment as of mid-April 2023. Additionally, NICA's exposures towards the productive sector, which includes agriculture sector, energy sector and micro, cottage, small and medium industries was 23.66% as of mid-July 2022 and 28.29%

² Source: Quarterly Published reports of Commercial Bank of Nepal

as of mid- April 2023). It is worth noting that the bank adequately lends to the deprived sector, accounting for 6.07% as of mid-April 2023.

Key Rating Weaknesses

Increased delinquency and NPL amid unfavorable economic environment

NICA's asset quality has experienced a significant decline, with delinquency levels increasing from ~46% as of mid-July 2022 to ~49% as of mid-January 2023 and further to ~51% as of mid-April 2023. This decline is mostly attributed to the implementation of working capital loan guidelines by NRB in mid-October 2022, which negatively impacted loan recovery processes and intended to discourage the practice of using loans to pay banks' interest. Additionally, NRB issued a directive on February 10, 2023, which prevented borrowers from being charged penal interest for a month from the date their outstanding loans became due until mid-June 2023. Despite the increase in Gross NPL ratio, which rose from 0.53% as of mid-July 2022 to 0.85% as of mid-April 2023, it remains lower than the industry average of 3.03%. However, the bank's provision for potential losses has decreased from 357% as of mid-July 2022 to 226% as of mid-April 2023, resulting in a decline in the solvency indicator (net NPL to net worth) from 0.76% as of mid-July 2022 to 2.71% as of mid-April 2023. Although the majority of the overdue portfolio is within the 1-30 days range, effectively managing the incremental slippage from the delinquent credit portfolio and improving asset quality will be crucial for the bank's profitability and capitalization, and is therefore a key rating sensitivity.

Modest liquidity profile

As of April 21, 2023, NICA has maintained a CRR of ~4.64% and a SLR of ~19.18% as of mid-April 2023, which complies with the NRB norms of 4% and 12% respectively. However, the bank's liquidity coverage ratio of 20.51% as of mid-April 2023, just meeting the minimum regulatory requirement of 20% remains a concern. Also, NICA's liquidity profile as of mid-April 2023 indicates negative cumulative mismatches within a year. This could lead to the bank borrowing at a higher cost to meet its obligations, potentially impacting its profitability and indicating potential liquidity risk. Therefore, it is crucial for the bank to effectively manage its assets and liabilities to ensure that it has enough liquidity to fulfill its obligations.

Intense competition

According to the monthly statistics published by the NRB for mid-March 2023, there are currently 21 Commercial Banks, including three major state-owned banks, operating in Nepal with a total of 5,049 branches. NICA has 359 branches (including head office) as of mid-March 2023. During 9MFY23, the industry (Class 'A' Commercial Banks) achieved a total interest income of ~NPR 409 Bn and a net interest income of ~NPR 138 Mn, with NICA's share being 7.04% (~NPR 29 Bn) and 6.69% (~NPR 9 Bn), respectively. The recruitment and retention of skilled manpower remains a major challenge to the banking industry amidst competition. Additionally, the unhealthy competition in interest rates, new technology-based services and growing demand among customers indicates a fresh challenge for the Nepalese banking sector.

Analytical Approach: Standalone

Applicable Criteria:

[Issuer Rating Methodology](#)

About the Company:

Incorporated in May 1997 as Nepal Industrial & Commercial Bank Ltd., NICA was later merged with Bank of Asia Nepal Ltd. on June 30, 2013 and was renamed as NIC Asia Bank Limited. It is a 'A' class Commercial Bank licensed from Nepal Rastra Bank (NRB). As of April 13, 2023, 93.07% of the bank's stake is held by individual and 6.93% by corporate entities (other than GoN and Licensed Institutions), with the promoter:

public stake of 51:49. The bank has been a certified by the International Organization for Standardization (ISO) and is accredited with ISO 27001: 2013 (Information Security Management System), which guarantees international standard information security.

Financial Indicators (Standalone)

For the year ended* As on	FY21	FY22	9MFY23
	Audited	Audited	Unaudited
Amount (in NPR Mn)			
Interest Income	23,562	32,772	28,777
Total Income	25,912	35,709	31,275
Interest Expenses	14,335	21,482	19,560
Net Interest Income	9,228	11,290	9,217
Profit After Tax	3,259	4,215	4,015
Deposits	287,025	289,904	316,545
Advances (Gross Figure)	267,279	271,632	283,219
Total Assets	346,056	358,437	364,639
Ratios			
Interest Rate Spread (%)	3.73	4.40	4.19
CASA (%)	39.49	40.27	39.48
Total CAR (%)	12.47	13.38	12.64
Tier-I Capital (%)	7.36	8.80	8.85
Gross NPL to Gross Advances (%)	0.50	0.53	0.85
Provision Coverage Ratio (%)	321	357	226
Cost of Funds (%)	5.30	7.39	7.97
Credit to Deposit Ratio (%)	87.58	89.85	84.85
Net Liquid Assets to Total Deposit (%)	20.65	20.30	20.51

Based on company's data

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About Infomerics Credit Rating Nepal Limited:

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