PRESS RELEASE

SALAPA BIKAS BANK LIMITED

January 2025

Ratings

Instrument/Facilities	Amount (NPR Mn)	Rating	Rating Action
Issuer Rating	NA	IRN B (Is)	Assigned
Total	**NA**		

Infomerics Credit Rating Nepal Limited (Infomerics Nepal) has assigned the issuer rating of IRN B (Is) [Single B (Issuer)]. Issuers with this rating are considered to have a high risk of default regarding the timey servicing of financial obligations.

Detailed Rationale

The rating assigned to Salapa Bikas Bank Limited (SBBL) is mainly constrained due to rapid deterioration in asset quality over the Q1FY25 whereby the GNPL ratio have reached 9.43% in comparison to 3.80% in FY24. The delinquencies in loan portfolio (overdue by more than 90 days) have almost tripled in past 3 months itself (NPR 83 Mn in Q1FY25 vis-à-vis NPR 30 Mn in FY24 end) leading to provision coverage ratio being halved (~59% in Q1FY25 vis-à-vis ~99% in FY24 end) and creation of hefty impairment charge of NPR 19Mn leading to a negative PAT of NPR 11 Mn in Q1FY25. Despite management citing financial illiteracy among borrowers for such elevation where loan is repaid in year-end only as evident by high GNPL in first quarter of previous years (8.41% in Q1FY24 and 7.79% in Q1FY23) and lowered GNPL at end of the same year (3.80% in FY24 and 3.11% in FY23), the ever increasing asset slippages across the years is a rating concern. The rating also remains constrained due to higher, albeit decreasing CASA[1] proportion of the bank across the years (~45% in Q1FY25 vis-à-vis ~53% in FY24 and ~63% in FY23). Despite the lowered CASA proportion resulting in a lowered cost of deposits (~6.5% in Q1FY25), it has led to stressed liquidity profile with negative cumulative mismatches except over 1 year indicating the need of bank to access funds at a higher cost of borrowings in case of emergency. The resulting is expected to cause a negative effect on SBBL's modest financial profile with SBBL merely making a profit over past years. (SBBL reported PAT of ~NPR 0.3 Mn in FY24 vis-à-vis negative PAT of NPR 3.2 Mn in FY23). The rating is also constrained due to high capitalization level (SBBL reported overall CAR of 28% in FY24 vis-à-vis ~24% in FY23 and ~41% in FY22) indicating inability of management to properly utilize its resources to generate higher returns. The rating is further weakened by its limited geographical coverage (SBBL is a one district operational development bank), higher operational expenses/total income ratio (~52% in FY24 vis-à-vis ~53% in FY23 and ~49% in FY22), lack of investment in other securities and small asset base. The rating also takes note of regulatory restriction on B Class Development bank to be involved in hypothecation loans, foreign currency based transactions and smaller capital base in comparison to commercial banks as a rating negative.

Nonetheless, the rating derives strength from SBBL's moderate track record of operations (since 2012 AD) coupled with experienced Board of directors and well-seasoned management team. The rating also takes a positive note of increasing advances and deposit albeit on a low asset base over the years. (CAGR of ~19% and ~16% across FY21-Q1FY25 respectively). The rating also takes positive note of SBBL's diversified credit portfolio, compliance with regulatory requirements related to disbursement of loans and granularity in loan portfolio as well as depositors.

Going forward, the company's ability to improve its asset quality alongside financial profile, leverage and utilize its capital structure to generate profit, maintain a stable liquidity profile and manage impact of other regulatory changes by NRB would remain key rating sensitivities.

[1] Current and Saving Account proportion

Detailed Description of Key Rating Drivers

Key Rating Strengths

Fair track record of operations coupled with experienced promoters and management team
Established in the year 2012 AD, SBBL has a fair track record of operation navigating in fairly dynamic and competitive environment. The bank's profile derives strength from its strong promoters who are well experienced in the banking and finance sector. SBBL is managed under the overall guidance of the bank's board of directors which includes eminent Businessmen/Industrialists with wide experience in the financial services. Mr. Tanka Rai is the Chairman of the bank, who has well over a decade of experience in banking and business sectors. The senior management team is experienced in their respective field of operations and is headed by chief executive officer Mr. Yogendra Pun, who has decades' worth of experience acting as province head of different commercial banks. He is aptly supported by an experienced management team.

Increasing scale of operations backed by consistent growth in deposits and stable growth in advances with diversified portfolio
SBBL deposits grew by a CAGR of 16.24% during FY21-Q1FY25 whereby the deposit base increased to NPR 1,114 Mn from NPR 683 Mn in FY21. Similarly, the loans and advances provided has also shown similar growth trajectory with it exhibiting CAGR of 19.39% during FY21-Q1FY25 whereby the same has increased to NPR 1,076 Mn from NPR 605 Mn in FY21. The consistent healthy increase in both asset and deposit base is a rating positive. In addition to such, the loans and advances portfolio has further been diversified by SBBL. At the end of Q1FY25, the proportion is concentrated at 30.73% for agriculture and forest related loan and 39.57% for other sector loans, followed by 9.22% towards wholesaler and retailer loan and 8.94% towards consumption loan. In recent years, SBBL has focused more on diversification of portfolio with concentration of agriculture loan reducing from 45.30% in FY22 to 30.73% in Q1FY25 and increasing concentration on other sector with it increasing to ~40% in Q1FY25 from 21% at the end of FY22. The effort of management to diversify its loan portfolio is quite commendable and the ability to continue to do so in near future is a rating monitorable.

Key Rating Weaknesses

Deteriorating asset quality
SBBL has faced rapid deterioration in asset quality over the first quarter of FY25 whereby the GNPL ratio have reached 9.43% in comparison to 3.80% in FY24. The delinquencies in loan portfolio (overdue by more than 90 days) have almost tripled in past 3 months itself (NPR 83 Mn in Q1FY25 vis-à-vis NPR 30 Mn in FY24 end) leading to provision coverage ratio being halved (~59% in Q1FY25 vis-à-vis ~99% in FY24 end) and creation of hefty impairment charge of NPR 19Mn leading to a negative PAT of NPR 11 Mn in Q1FY25. GNPL had been historically high in first quarter of previous years too (8.41% in Q1FY24 and 7.79% in Q1FY23) primarily attributable to financial illiteracy and misconception among the borrowers that loan repayment is only necessary towards year end only as evident by reduction in GNPL at end of each year (3.80% in FY24 and 3.11% in FY23). The existing pattern of decreasing GNPL at year end provides some comfort regarding prospective GNPL at the end of FY25 too. However, the ever increasing asset slippages across the years (GNPL of 3.80% in FY24 vis-à-vis 3.11% in FY23 and 3.53% in FY22) is still a rating concern. The ability of management to reduce it asset slippages while expanding its operation and asset base is a key rating sensitivity.

High capital adequacy level
SBBL's overall Capital Adequacy Ratio (CAR) stood at 33.56% as on Mid-April 2024, (29.34% as on Mid-July 2024 and 24.59% as on Mid-July 2023) as against regulatory requirement of 11%. Further, overall CAR remained high and have remained stable during FY23-24 after CAR reduced from 42.50% in FY22 due to increase in risk weighted exposures. Having a high CAR compared to the industry average (13.53% as on Q1FY25) may also indicate that the bank is not effectively utilizing its capital.

This can be a concern from credit rating perspective as it indicated SBBL's inability to utilize its capital to generate higher returns to some extent. With further capital of NPR 172 Mn being issued to the public, the ability of management to effectively utilize its capital to generate returns is key monitorable.

Higher proportion of CASA resulting in large interest spread and stressed liquidity challenges to SBBL

SBBL's CASA ratio, although significantly higher than the industry average, has been on a declining trajectory in recent years, reaching 45.02% in Q1FY25 from 53.09% in FY24, 63.07% in FY23, 69.35% in FY22, and 71.89% in FY21. This remains notably above the industry average of 36.18% in Q1FY25 and 25-30% during FY21-24, primarily due to the historically low level of fixed deposits. The high CASA proportion supports a lower-cost funding base, as reflected in the sizable interest rate spread of 6.77% in Q1FY25 compared to ~10.24% in FY22. However, the high CASA dependency has contributed to liquidity challenges, with net cumulative mismatches across short-term buckets (except beyond one year), potentially compelling the bank to raise higher-cost funds to meet short-term obligations in times of stress which if occurred can cause severe consequences given SBBL's weak financial profile with SBBL reporting PAT of ~NPR 0.3 Mn in FY24 vis-à-vis negative PAT of NPR 3.2 Mn in FY23. SBBL has adhered to regulatory norms with a CRR of ~7.39% as of FY24 end (against NRB's 4% requirement) and an SLR of 41.86% as of FY24 end (against the 12% minimum). Its liquidity coverage ratio (LCR) stood at 49.50% as of mid-July 2024 (~64.26% as of mid-July 2023), reflecting stable compliance with liquidity metrics.

Intense Competition and regulatory restrictions

Currently there are 17 Development Banks, including eight nationwide development banks, nine regional development banks among which 6 operates in 1-5 district, 1 each operates in 1-3 district, 1-7 district and 1 district respectively. These banks cumulatively account for 1,137 branches and supports ~7.2 Mn Deposit accounts and 0.28 Mn loan accounts (based on Monthly statistics published by NRB for Mid-Nov 2024). SBBL is a 1 district regional development bank based in Khotang with 6 branches along with head office as on same date. Industry (Class 'B' Development Banks) has achieved total interest income of ~NPR 20.28 Bn during November 2024 with ~NPR 7.63 Bn net interest income; SBBL's share on interest income is 0.22% (NPR 44 Mn) and 0.29% share on net interest income (NPR 22 Mn) for the same period. The Development Bank sector faces several challenges, including intense competition in interest rates, regulatory restrictions imposed prohibiting development banks from foreign currency transactions and hypothecation loan borrowings among others. Additionally, development banks face competitive disadvantages due to their smaller capital base and more limited reach compared to commercial banks. Emerging challenges also include the growing demand for technology-driven services and the need to adapt to rapidly evolving customer expectations in the digital age.

Analytical Approach: Standalone

Applicable Criteria:

Bank Rating Methodology

About the Company:

Salapa Bikas Bank Limited (SBBL) is a one-district regional development bank based in Khotang with 6 branches along with head office as on October 15, 2024. SBBL is a "B" Class Development Bank licensed by Nepal Rastra Bank (NRB). SBBL was incorporated on July 16, 2012 and started commercial operation from 2012 itself. SBBL is promoted by individuals from various backgrounds and Mr. Dhan Prasad Rai (0.61%) and Mr. Manindra Rai (0.50%) are the major shareholders of SBBL as on Mid-October 2024. SBBL has a paid up capital of NPR 350 Mn as on same date and its entire shareholding is held by promoters themselves.

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Financial Indicators (Standalone):

(NPR Mn)

For the year ended* As on	FY21	FY22	FY23	FY24	Q1FY25
	Audited	Audited	Audited	Unaudited	Unaudited
Interest Income	82	105	127	138	33
Total Income	89	111	133	143	37
Interest Expenses	37	48	67	65	16
Net Interest Income	45	57	60	72	17
Profit After Tax	4.6	14.6	-3.2	0.3	-10.9
Deposits	683	776	787	886	1,114
Advances (Gross Figure)	605	680	830	982	1,076
Total Assets	1,004	1,351	1,366	1,443	1,507
Ratios					
Interest Rate Spread (%)	8.45	10.24	9.24	8.46	6.77
CASA (%)	71.89	69.35	63.07	53.09	45.02
Total CAR (%)	27.49	41.38	23.79	28.41	33.56
Tier-I Capital (%)	28.85	42.50	24.59	29.34	NA
Gross NPL to Gross Advances (%)	8.29%	3.53%	3.11%	3.80%	9.43%
Provision Coverage Ratio (%)	80.57	112.70	121.19	98.53	58.97
Cost of Funds (%)	5.04	5.99	7.48	6.61	6.00
Credit to Deposit Ratio (%)	88.62	87.61	105.57	110.87	96.64
Net Liquid Assets to Total Deposit (%)	54.39%	80.04%	64.26%	49.50%	37.28%

**** Classification as per Infomerics Nepal Standard***

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About Infomerics Credit Rating Nepal Limited:

Infomerics Credit Rating Nepal Ltd. is Nepal's third Credit Rating Agency licensed by the Securities Board of Nepal (SEBON) on March, 2022. Infomerics Nepal is a subsidiary of Infomerics Valuation and Rating Private Limited (Infomerics India) which is a SEBI registered and RBI accredited Credit Rating Agency licensed in 2015. Infomerics Nepal aims to provide investors with objective analysis and evaluation of credit worthiness of Banks, NBFCs, Large Corporates and Small and Medium Scale Units (SMUS) via its rating and grading services. Thus, it is playing a key role in serving the financial markets by reducing the information asymmetry among varied lenders and investors and facilitating borrowers/issuers to various fundraising opportunities/avenues. Infomerics observes and maintains ethical standards in its activities. For more information, visit https://infomericsnepal.com/

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