NMB Bank Limited

ICRA Nepal assigns [ICRANP] IPO Grade 3 to the proposed further public offerings (equity shares) of NMB Bank Limited

Facility/Instrument	Issue Size	Grading Action
Further Public Offer (FPO) (Equity)	NPR 3,801.2493 million	[ICRANP] IPO Grade 3 (*Assigned on Jan 2018 and revalidated with FPO price update on June 2018*)

ICRA Nepal has assigned "[ICRANP] IPO Grade 3", indicating average fundamentals to the proposed rights issue amounting to ~NPR 3,801.25 million of NMB Bank Limited (NMB). ICRA Nepal assigns IPO[1] grading on a scale of IPO Grade 1 through IPO Grade 5, with Grade 1 indicating strong fundamentals and Grade 5 indicating poor fundamentals. For the grading categories 2, 3 and 4, the sign of + (plus) appended to the grading symbols indicate their relative position within the grading categories concerned. Thus, the grading of 2+, 3+ and 4+ are one notch higher than 2, 3, and 4, respectively. NMB has proposed further public issue of 11,415,163 units of equity shares of face value NPR 100 each at a premium of NPR 233 (issue price of NPR 333 per share). The issue is being made to comply with the increased paid up capital requirement[2] set by Nepal Rastra Bank (NRB), the banking sector regulator in Nepal.

The average fundamental grading factors in NMB's established track record (operating since 1996[3]), good franchise network (97 branches as on mid-Apr 2018) and adequate market share (~3.2% share in the banking industry credit and deposits) which results in good market positioning. Good market positioning coupled with comfortable capitalization profile and experienced senior management augurs well for incremental growth prospects of the bank. The grading also factors in healthy rate of business growth (aided by merger with regional banks and financial institutions in October 2015) and profitability maintained in past years. The grading also factors in NMB's good assets quality (gross NPLs of 1.20%[4] on mid-Jan 2018) and relatively low credit concentration risk. The grading also considers diversified earnings profile (non-interest income of 1.5% of ATA in past ~2 years) of NMB. The grading also factors in high institutional shareholding in NMB of 35% (including 20% stake from FMO[5]) which adds to the governance profile of the bank.

However, the grading remains constrained by moderate funding profile of the bank vis-à-vis industry; as characterised by inferior CASA mix (33% as on mid-Jan 2018 vs. commercial bank average of ~43%) and relatively higher deposit concentration (34% of deposits among top 20 accounts as on mid-Oct 2017). Due to higher reliance on price sensitive high-ticket deposits, NMB fares inferior to the industry leaders in terms of cost of fund and base rate. This could be a competitive disadvantage in the "base rate plus" lending model recently implemented in the industry. NMB has underwritten/ acquired sizeable credit portfolio during low interest rate regime of FY2013-FY2016; which could come under stress in rising interest rate scenario seen in recent period. The grading is also constrained by uncertain operating environment that the banks in Nepal are currently facing.

NMB's credit portfolio has grown at a healthy pace of CAGR ~38% over past 5 years ending FY17, albeit on a low base. The credit growth was aided by merger with 4 regional BFIs in October 2015. The growth in the post-merger era has remained low (~15% growth in FY17) due to focus on the portfolio consolidation and shortage of lendable funds in the banking industry that developed towards second half of FY17. Given the deposit crunch, incremental credit growth of the bank is likely to remain pegged with the incremental deposit growth. Management's ability to mobilize the adequate franchise network of the bank to generate fresh deposits remains to be seen. As on mid-Oct 2017, NMB's credit portfolio stood at NPR 64 billion; broadly comprised of loan towards Small and Medium Enterprise (SMEs) (40%), towards large corporates (35%) and retail consumer loans (19%). NMB's credit concentration has grown

[1] Includes grading of IPO, rights issue and further public issue.
[2] NPR 8 billion for class A commercial bank.
[3] As class C finance company before its upgradation to Class A bank in 2008.
[4] Gross Non-Performing Loan as on mid-Apr-18 is 1.10% as per unaudited report
[5] FMO is a bilateral Development Bank based in Netherland with 51% stake by the Dutch State.

marginally during past 12-18 months yet remains comfortable (23% of total credit among top 20 borrower groups). Assets quality of NMB remains good with gross NPLs of 1.20% on mid-Jan 2018 (1.68% on mid-July 2017) and 0+ days delinquency of ~6% on mid-Oct 2017.

In terms of deposit profile, NMB continues to fare weaker to the industry average. As on mid-Jan 2018, NMB's deposit base of NPR 80 billion comprised of 33% CASA (lower than industry average of ~43%), at par with mid-July 2017 level and lower to mid-July 2016 level of ~36%. At the same time, deposit concentration among top accounts remains on higher side. During past 12-18 months, Nepalese banking industry has witnessed shortage of lendable deposits pushing up the cost of deposits. This is likely to adversely affect the bank's competitive positioning (in the "base rate plus" lending rate regime). This is also likely to affect NMB's profitability (by affecting the net interest margin) as the bank's ability to pass on the increased cost to the borrower is dictated by industry competition. CCD ratio of NMB remains comfortable despite moderation in deposit growth vis-à-vis credit growth in recent years (~76% on mid-Jan 2018 vs. regulatory ceiling of 80%).

As for profitability, NMB's average return on net worth (~19% over past 2-3 years) remains above commercial bank average; albeit partly aided by reversal of credit provisions maintained at the time of merger. Profitability also remains supported by fair Net Interest Margin (NIMs) (~3% of average total assets (ATA)) on growing asset base. NIMs in turn remains supported by healthy yield on advances on retail/SME dominated lending portfolio and healthy rate of credit mobilisation (CCD ratio of 75-78% during past 1-2 years). Non-interest income of NMB has improved in the post-merger era (~1.5% of ATA) diversifying the earnings profile. Profitability also remains supported by low credit provision expenses. However, due to slow growth post-merger, operating expense ratio continues to remain high (~1.9% of ATA) which remains a drag to profitability. Going forward, bank's profitability will depend on its ability to achieve targeted growth by managing required funds and maintain assets quality on current and incremental credit portfolio.

NMB's capitalization profile improved in FY17 after fresh equity injection from FMO, pushing up the capital adequacy ratio (CRAR[6]) from ~11% to ~13%. As on mid-Apr 2018, NMB's CRAR stood at 12.92%, comfortable vis-à-vis regulatory minimum of 11% under prevailing Basel III norm. NMB's tier I capital (11.84% as on mid-Apr 2018) remains well above 8% to be maintained by mid-July 2018 and 8.50% to be maintained by mid-July 2019 under the Basel III norms prescribed by NRB. Capitalisation of proceeds from proposed FPO is likely to give further boost to the capitalization profile of the bank (assuming full subscription) and improve the risk bearing capacity of the bank. Post-FPO, NMB's paid up capital will be ~NPR 0.4 billion short of revised regulatory requirement of NPR 8 billion; which will be met through the capitalisation of retained earnings.

Bank Profile

NMB Bank Ltd started its operation from 26th December 1996 as a Class C Finance Company. The bank has been operating as a commercial bank following its up gradation from Class C to Class A in May 2008. It was registered as joint –Venture Company with foreign promoter M/s Young Leon Realty, Malaysia. In the first half of FY 2015-2016, NMB underwent merger with 4 regional banking and financial institutions[7] to raise the minimum paid up capital, commencing joint operation from mid-October 2015. The merger increased the capital fund and assets base of NMB in addition to increasing its footprint across the country.

Post-merger NMB issued further promoter equity shares to FMO Netherland. This increased FMO's stake in NMB to 20% from 3.18% immediately following the merger[8]. As on mid-Jan 2018, promoter public shareholding of NMB stood at ~60:40. The current major promoter group of the bank includes FMO (20% shareholding), Employee's Provident fund (~8%) and Young Leon Realty (~6%) with remaining promoter stake held mostly by individual businessmen and private investment companies.

---

[6] Capital to risk-weighted-assets adjusted ratio

[7] **Clean Energy** Development bank (CEDBL-National Level Class B Bank), **Bhrikutee** Development Bank (10-district level Class B Bank-graded IPO 3 by ICRA Nepal in November 2014), **Pathibhara** Development Bank (3-district level Development Bank) and P**rudential** Finance Limited (National Level Class C Finance Company)

[8] FMO was the major promoter in one of the merging entities (Clean Energy Development Bank).

As on mid-Apr 2018, NMB has presence throughout the country through its 97 branches. NMB has market share of about 3.2% in terms of deposit base and 3.2% of total advances of Nepalese Banking Industry as on mid-Jul 2017 (~3.6% and ~3.7% share among the commercial banks). NMB reported a profit after tax of NPR 1,511 million during FY 2016-17 over an asset base of NPR 86,867 million as at mid-Jul-17 against profit after tax of NPR 1,115 million during FY 2015-16 over an asset base of NPR 74,613 million as on mid-Jul-16. Till mid-Apr-18 (Q3FY 2017-18), NMB has reported a net profit of NPR 1,410 million over an asset base of NPR 102,154 million. As of mid-Apr-18, NMB's CRAR[9] was 12.92% (tier I CRAR 11.84%) and gross NPLs were 1.10%.

June 2018

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

[9] Capital to risk-weighted-assets adjusted ratio