Muktinath Bikas Bank Limited

Rating

Facilities	Amount (Rs. in Million)	Ratings[1]	Rating Action
Issuer Rating	**NA**	**CARE-NP BBB (Is) [Triple B (Issuer Rating)]**	**Reaffirmed**

CARE Ratings Nepal Limited (CRNL) has reaffirmed the issuer rating of 'CARE-NP BBB (Is)' [Triple B (Issuer Rating)] assigned to Muktinath Bikas Bank Limited (MNBBL). Issuers with this rating are considered to offer moderate degree of safety regarding timely servicing of financial obligations, in Nepal. Such issuers carry moderate credit risk.

Detailed Rationale & Key Rating Drivers

The reaffirmation of the issuer rating assigned to MNBBL derives strength from its established track record of operations, experienced board and management team supported by diversified geographical coverage and adequate capitalization levels. The rating also factors in satisfactory financial performance in so far in FY25 (FY refers to the twelve-month period ending mid-July), moderate CASA ratio and moderate liquidity profile. The rating, however, is constrained by MNBBL's declining asset quality over FY24 and so far in FY25. The rating also factors in the bank's exposure to the regulatory risk. Subdued scope for credit growth over the near-term and elevated provisioning requirements in the current market dynamics are likely to add to the margin pressure of the bank over the near term. Although current capitalization levels remain adequate, further slippages in asset quality leading to GNPL levels significantly higher than envisaged will remain a key rating monitorable.

Going forward, the ability of the bank to manage growth while maintaining profitability levels and without compromising on asset quality would be critical for the bank's earning profile. The bank's ability to improve capital adequacy indicators with comfortable cushion from the minimum regulatory requirement levels, and manage the impact of any other regulatory changes by Nepal Rastra Bank (NRB) would be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Established track record, experienced board and management team and diversified geographical coverage

Operating since 2007, MNBBL has more than 17 years of operational history and an established market presence in Nepal. MNBBL is a professionally managed bank under the overall guidance of the Board of Directors (BoD) which includes professionals with wide experience in the financial and economic sector. Mr. Khim Prasad Malla is the Chairman of MNBBL. The management team is led by Mr. Pradyuman Pokharel, Chief Executive Officer, who has around three decades of experience in banking sector and is aptly supported by an experienced management team.

MNBBL has diversified geographical presence in Nepal with 179 branches and 22 ATMs as on mid-January 2025 across the country. The branches are spread over all seven provinces of Nepal.

Adequate capitalization levels

Tier I Capital Adequacy ratio of the bank improved to 9.79% as on mid-Jan 2025 from 9.46% as on mid-July 2024 (minimum requirement of 8.5% for national level Class-B Banks and Financial Institutions from mid-July 2024) and Overall

[1] Complete definitions of the ratings assigned are available at www.careratingsnepal.com and in other CRNL publications

Capital Adequacy ratio slightly increased to 11.87% as on Mid-Jan 2025 from 11.69% as on mid-July 2024 (minimum requirement of 11%). The central bank of Nepal has increased regulatory capital to 8.5% and 11% (Tier I and total CAR, respectively) from mid-July 2024 from 6% and 10% earlier. The slight improvement in Tier I levels and overall capital adequacy ratio of the bank in H1FY25 was mainly on account of increased core capital of the bank as on mid-Jan, 2025 supported by internal capital generation despite loans and advances portfolio increasing by 4.57%. The profitability of the bank has improved in H1FY25 as indicated by net profit of Rs. 503 Mn in H1FY25 (H1FY24: Rs. 420 Mn) mainly on account of decrease in interest expenses. The bank's ability to manage asset quality and growth in business while maintaining enough cushion in its capitalization levels will remain critical from credit perspective. The bank is in process of issuing perpetual preference shares of Rs. 1000 Mn, which is expected to provide additional cushion to its capitalization levels.

Satisfactory financial performance

During FY24, the MNBBL's total income decreased by 10.70% year-on-year to Rs. 14,370 Mn during FY24 which was Rs. 16,091 Mn during FY23. The decrease is mainly on account of lower yield on advances on loans and advances during FY24. Nonetheless, the bank was able to report 3.29% y-o-y growth in net interest income during FY24 (FY23: Rs.4,104 Mn and FY24: 4,239 Mn). Pre-Provisioning Operating Profit (PPOP) remained relatively stable i.e. Rs. 2,509 Mn and Rs. 2,459 Mn during FY23-FY24. Impairment losses (loan loss provisioning) increased by ~11% y-o-y to Rs. 777 Mn during FY24 amid rise in NPL and delinquency levels. The net profit of the company thus declined by 5.8% y-o-y to Rs. 1,176 Mn during FY24 on account of higher impairment charges amid increasing GNPL levels. Consequently, ROTA declined to 0.92% in FY24 from 0.99% in FY23. During H1FY25, total income declined by 23.03% year-on-year to Rs. 5,939. However, Net Interest Margin (NIM) increased to 3.47% in H1FY25 (H1FY24: 3.23%). Net profit increased to Rs. 503 Mn in H1FY25 from Rs. 420 Mn in Q1FY24 amid decline interest expenses.

Moderate CASA ratio

MNBBL maintained 33.40% CASA deposits in FY24, marginal improvement from 24.64% in FY23 compared to industry average of 30.86% and 34.37%, respectively. The higher CASA ratio led to decreased cost of funds at 6.54% in FY24 resulting into base rate of 8.78% in FY24. Lower cost of funds against its peers imposes competitive advantage for the bank, especially in the "base rate plus lending rate" regime. CASA deposits were higher in FY23-FY24 industry-wide with lower proportion of current deposits and higher proportion of fixed deposits as compared to previous quarters. MNBBL's CASA proportion improved in H1FY25 to 36.58%. The bank's ability to maintain the improving trend in CASA mix leading to favourable cost of funds vis-à-vis peers for a sustained period remains to be seen.

Moderate liquidity profile

MNBBL has a moderate liquidity profile marked by Cash Reserve Ratio (CRR) of 4.38%, Statutory Liquidity Ratio (SLR) of 20.20% and Net Liquidity Ratio of 22.88% as on mid-January 2025 (CRR: 4.02%, SLR: 22.56% and Net Liquidity Ratio: 24.01% as on Mid-July, 2024) against regulatory requirement of 4%, 10% and 22% respectively which remain satisfactorily above the regulatory norms. Furthermore, the bank's liquidity profile remains moderate from the asset-liability mismatch perspective with positive cumulative mismatches as of mid-January 2025.

Key Rating Weakness

Weak asset quality

Although MNBBL continues to exhibit better asset quality profile vis-à-vis industry peers, its Gross Non-Performing Loans (GNPL) levels have spiked to around 3.98% as on mid-Jan 2025 compared to 2.26% as on mid- July 2024. MNBBL has historically maintained a relatively better asset quality profile vis-à-vis the industry reflective of the bank's more efficient risk management setup. MNBBL had GNPL ratio of 3.98% as on mid-Jan 2025, compared to the industry average of 4.79% for class B financial institutions. The decline in asset quality of MNBBL and the overall banking industry over FY24 and so far in FY25 can be attributed to sluggish economy coupled with low capital expenditure by the government. However, some comfort is taken in MNBBL displaying a more resilient asset quality relative to peers. MNBBL's ability to improve the asset quality indicators going forward would remain a key rating monitorable.

Competition from other banks and financial institutions

Currently there are 17 Development Banks, operating with total 1,132 branches all over Nepal (based on monthly statistics published by NRB for mid-January 2025). MNBBL has 179 branches along with head office as on same date. Industry (Class B Development Banks) had achieved total interest income of Rs. 29,332 Mn during H1FY25 with Rs. 10,884 Mn net interest income; MNBBL's share on interest income is 19% (Rs. 5,574 Mn) and 20.15% share on net interest income (Rs. 2,194 Mn) for the same period. MNBBL's share on interest income decreased from 20.66% to 19.55% in FY23 however, share on net interest income increased to 19.59% in FY24 from 19.26% in FY23. Despite being established national development bank in the industry, it is challenging for MNBBL to maintain current market share and expand its business, due to high competition among bank and finance companies, existence of large number of Development bank along with Commercial banks and finance companies conducting similar kind of businesses and they lend at lower interest rate as well as they offer wider banking services than development banks.

Exposure to regulatory risk related to industry

The Banking and Finance industry in Nepal is exposed to changes in the various regulatory measures issued by NRB from time to time. In past, finance companies faced pressure from NRB for capital increment to Rs. 800 Mn from Rs. 200 Mn. NRB had changed the minimum regulatory capital of national level development banks from FY24 end onwards. National levels development banks are required to maintain tier 1 capital adequacy ratio of 8.5% and overall, CAR of 11% from mid-July 2024 onwards, which is in line with the requirement for Class A commercial banks in Nepal. Furthermore, NRB had changed to CD ratio mechanism from existing Credit to Core Capital plus Deposit (CCD) ratio measures. CD ratio needs to maintain below 90% from mid-July 2022 from earlier provision of 85% for CCD. Risk weights of certain loans including personal overdrafts, TR loans, hire purchase loans for personal purpose, margin lending, etc. have been fluctuating between 100% to 150% via interim changes in monetary policies by the NRB. Unfavourable changes depending on the bank's exposures are likely to put downward pressure on capital adequacy ratios of the MFIs and limit their ability for significant credit expansion, at least over the near term. Furthermore, increased interest rates will likely put upward pressure on both lending and deposit interest rates of the MFIs over the near term.

About the Company

Muktinath Bikas Bank Limited (MNBBL) is a national level class "B" Development bank and started its commercial operations from January 07, 2007. MNBBL was upgraded into a national level development bank in July 2015 after acquisition of Civic Development Bank. The bank is listed on Nepal stock exchange and promoter and public shareholding was in the ratio of 51:49 as on Mid-July, 2022.

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