

## ICRA Lanka assigns [SL]AAA rating with Stable outlook to National Savings Bank

June 24, 2019

Instrument	Rated Amount (LKR Mn)	Rating Action
Issuer rating	N/A	[SL]AAA (Stable) Assigned

### Rating action

ICRA Lanka Limited, subsidiary of ICRA Limited, a group company of Moody's Investors Service, has assigned the issuer rating of [SL]AAA (Pronounced SL triple A) with Stable outlook to National Savings Bank (NSB or the Bank).

### Rationale

The rating takes note of the 100% Government of Sri Lanka (GoSL) ownership, which provides a strong likelihood of sovereign support and, the 100% explicit guarantee provided by the Government of Sri Lanka (GoSL) for the moneys deposited with the Bank and the interest thereof through the National Savings Bank Act (NSB Act). The rating factors in the low risk investment portfolio, good quality lending portfolio and the presently adequate capital profile. The earnings of the Bank moderated as a result of derecognition of LKR 3.6 Bn as net income earned from the government securities transactions from April 01, 2019 as a result of removal of Withholding Tax from government securities transactions. The Bank's investment portfolio is characterised by low risk, with NSB mandated to invest a minimum of 60% of the total deposits in government securities; as in March 2019, 62% of the deposits was in government securities. The quality of the lending portfolio is driven by zero NPAs reported on its exposure to GoSL, SOE<sup>1</sup> and corporate portfolio which accounted for 41% of the lending portfolio. The standalone gross NPA ratio (GNPA %) of the retail portfolio (59% of lending portfolio) stood at 2.46% as of Dec-18. NSB's BASEL III complied total capital adequacy ratio (CAR) stood at 15.43% (Tier-I capital ratio at 12.81%) as compared to 14.00% (Tier-I capital ratio at 10.00%) regulatory requirement as of Mar-19. ICRA Lanka notes that moderation in internal generation will require the Bank to secure commensurate capital from GoSL in the medium term. Going forward, maintenance of adequate buffers (at least 1%) over and above the minimum capitalisation requirements (Tier-I plus CCB and total CAR) would be critical for sustenance of the current rating.

### Outlook: Stable

ICRA Lanka believes that NSB will continue to benefit from Government support because of its systemic importance considering its position as the largest licenced specialised bank in Sri Lanka, which also provides vital funding support to GoSL as per the NSB Act. The outlook may be revised to 'Negative' in case of a steady shortfall in NSB's capital buffers over the regulatory requirements as compared to ICRA Lanka's expectations or in case of further weakening in the profitability and asset quality indicators.

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<sup>1</sup> SOE – State Owned Entity

## Key rating drivers

### Credit strengths

**100% government ownership and explicit guarantee on deposits:** NSB is a 100% government owned specialised bank incorporated under the NSB Act in 1972. The main objective of the Bank is to promote savings habit in the country. GoSL provides explicit 100% guarantee through the NSB Act for the depositors' deposit money and the interest there on. Since the Bank's inception, NSB has been able to self-fund its capital requirements and has not required any capital support from GoSL. ICRA Lanka expects GoSL's support, if needed, given the Bank's position of being a systemically important bank and also being one of the important sources for its financing needs. The Government appointed board comprises of a mix of qualified and experienced professionals, including representative from the treasury and the Post Master General. The senior management of the Bank consists of qualified and experienced banking professionals.

**Low risk nature of its investment portfolio:** The Bank is mandated to invest a minimum of 60% of the deposits in government securities. As of Mar-19, 62% of the total deposits were invested in government securities, as compared to 61% as of Dec-18 (75% as of Dec-17). ICRA Lanka noted a gradual reduction in the share of government securities since Dec-17, largely as a result of maturity of its LKR 64 Bn investment in Sri Lanka Development Bonds in Sep-18 and due to diversification to lending portfolio to optimise its overall yields. As of Mar-19, 93% of the investment portfolio consisted of Treasury Bills and Bonds followed by 4% in placement with banks, 2% in Debentures and Trust Certificates, 1% in listed equity and the balance as investment in subsidiaries, unquoted equities and others. As of Dec-18, close to 97% of the government security portfolio was classified as AC<sup>2</sup> and balance as FVPL<sup>3</sup> and FVOCI<sup>4</sup>. The Bank's FVPL equity portfolio reported significant mark to market losses where the market value was LKR 1,879 Mn as compared to the cost of LKR 3,368 Mn as of Dec-18. Since the equity portfolio represents less than 1% of the total investment portfolio, overall impact on the investment portfolio is expected to be minimal.

**Healthy overall asset quality supported by zero NPAs on corporate and GoSL & SOE portfolios;** NSB reported LKR 444 Bn lending portfolio as of Mar-19 as compared to LKR 424 Bn as of Dec-18 (LKR 376 Bn as of Dec-17). The portfolio reported an annualised growth of 19% in the latest quarter ended Mar-19 as compared to 13% growth in CY2018 (16% in CY2017). The portfolio growth in Q1CY2019 was driven by the retail lending which grew from LKR 250 Bn in Dec-18 to LKR 261 Bn in Mar-19. As of Mar-19, NSB's portfolio included retail exposure which contributed to 59%, followed by, Government and SOE at 32% and corporate at 9%. Under the retail segment, personal loans, housing loans, pawning and loans against FDs represented 29%, 15%, 7% and 7% respectively of the total portfolio as of Mar-19. Based on NSB's Act, all the SOE loans are secured by government guarantees and are routed through the Treasury, which further strengthens the credit profile of the lending portfolio. The Bank reported a gross NPA ratio of 1.44% as of Dec-18 as compared to 1.34% as of Dec-17, it remained at 1.45% as of Mar-19. ICRA Lanka noted that corporate and government & SoE portfolios of the Bank which accounted for 41% (Mar-19) of the total

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<sup>2</sup> Financial assets measured at amortised cost

<sup>3</sup> Financial assets measured at fair value through profit or loss

<sup>4</sup> Financial assets measured at fair value through other comprehensive income

lending portfolio had zero NPAs; ICRA Lanka envisages the same going forward. The retail portfolio of the Bank reported a GNPA% of 2.46% as of Dec-18 as compared to 2.39% as of Dec-17. At the product level, Auto Loans reported a GNPA% of 8.13% followed by Personal loans at 3.32%, Housing loans at 2.65% and Pawning at 0.77% as of Dec-18. ICRA Lanka expects the Bank to maintain its GNPA% below the systemic averages going forward. The Bank's IFRS based provision coverage ratio improved to 63% as of Dec-18 from 55% as of Dec-17 with the implementation of IFRS 9 standards.

**Granular deposit base;** NSB reported a deposit base of LKR 862 Bn as of Mar-19 as compared to LKR 840 Bn reported as of Dec-18 (LKR 737 Bn as of Dec-17). The NSB Act provides explicit government guarantee for the deposits and interest payable thereon. The Bank has a granular deposit base with the top 10 depositors accounting for 0.3% of the total deposits. The Bank's short term (less than 1 year) ALM mismatch was negative 71% as of Mar-19 as a result of its shorter tenured deposits as against longer tenured loan portfolio. The Bank's Liquidity Coverage Ratio stood at 309% as of Mar-19 as compared to the regulatory requirement of 100%. The Bank's significant investment in government securities provides comfort on the liquidity.

**Adequate capital profile;** NSB reported a Tier-I Capital Ratio of 12.81% and total capital ratio of 15.43% as of Mar-19 as compared to the regulatory requirement of minimum Tier-I Capital Ratio of 10.00% and total capital ratio of 14.00%. The Bank's core capital stands at about LKR 30 Bn as compared to the LKR 7.5 Bn regulatory core capital threshold to be achieved by December 31, 2020. Based on ICRA Lanka's computation, the Bank will require a Tier-I capital infusion of LKR 1.0-1.2 Bn in next 3 years to maintain a 10-15% growth factoring a 2% capital buffer and 8% internal capital generation. ICRA Lanka believes that as a systemically important bank, the government of Sri Lanka will provide the required funding support to the Bank when needed. Going forward, maintenance of adequate buffers (at least 1%) over and above the minimum capitalisation requirements (Tier-I plus CCB and total CAR) would be critical from a rating perspective.

## Credit challenges

**Moderating profitability indicators;** NSB's NIM moderated to 2.43% in CY2018 from 2.61% in CY2017 as a result of removal of With Holding Tax on government securities in Apr-18. In Q1CY2019, NIM improved with the repricing of the matured investments in government security portfolio. The Bank reported a trading loss of LKR 707 Mn in CY2018 as compared to LKR 1,206 Mn profit in CY2017. The trading loss was due to mark to market loss in the equity portfolio. ICRA Lanka noted that, in CY2017, the Bank's subsidiary NSB Fund Management Company Limited declared LKR 750 Mn dividend which supported the profit reported in the same period. The Bank's PAT dropped to LKR 4.5 Bn in CY2018 as compared to LKR 9.7 Bn reported in CY2017. The main reason was due to removal of withholding tax from the government securities, which resulted in non-recognition of income of close to LKR 3.6 Bn. The Bank reported a RoA of 0.85% in Q1CY2019 as compared to 0.78% in CY2018 (1.47% in CY2017).

**Analytical approach:** For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.  
**Links to applicable criteria:** [ICRA Lanka's Credit Rating Methodology for Banks](#)

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## About the entity:

National Savings Bank (NSB) was established in 1972 through the Parliament Act, No.30 of 1971 by amalgamating the Ceylon Savings Bank, the Ceylon Post Office Savings Bank, the savings certificate section of the Post Master General's Department and the Ceylon War Savings movement. Currently, NSB operates with 255 branches and a network of over 4,000 post offices as at March 31, 2019. The Bank's sole subsidiary, NSB Fund Management Co. Ltd is a dedicated primary dealer.

During the CY2018, NSB reported a PAT of LKR 4,500 Mn on a total asset base of LKR 1,037 Bn as compared to a PAT of LKR 9,716 Mn on a total asset base of LKR 1,011 Bn in the previous financial year. For 3MCY2019, NSB reported a PAT of LKR 1,196 Mn on a total asset base LKR 1,069 Bn.

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