

INITIAL PUBLIC OFFERING

Report Date: 2075/01/12

Nepal Seva Laghubitta Bittiya Sanstha Limited

Recommendation – Apply

SECTOR: RETAIL MICRO CREDIT

Listing Range: Rs. 103-311

Introduction of the Company

Nepal Seva Laghubitta Bittiya Sanstha Limited is a “D” class financial institution licensed by Nepal Rastra Bank. It was registered as Public Limited Company on 2070/08/16. It has been in operation from 2071/08/08.

The registered office of the company is situated at Melamchi Municipality-13, Fatakshila, Sindhupalchowk, Nepal.

Area of Operation

The company has license to operate in 3 districts that includes Sindhupalchowk, Nuwakot, Rasuwa.

Branch Extension

The company is operating through 8 branches in 3 districts. The company projects to increase its branch offices in future days.

Members Details

There are 5,461 members as of FY 2073/74.

Utilization of IPO Proceeds

The IPO proceed is projected to be utilized under;

- Animal Husbandry and Agricultural Loan: NPR. 10,000,000
- Retail Business & Services Loan: NPR. 5,000,000
- Small & Domestic Industries Loan: NPR. 3,000,000

Issue Details

Issue Size (Kitta)	180,000
Price per Share (NPR)	100
Issue Open Date	2075/01/12
Issue Close Date	2075/01/16
Issue to Staff (2%) (Kitta)	3,600
Issue to Samuhik Lagani Kosh (5%) (Kitta)	9,000
Issue to General Public (Kitta)	167,400
Issue Manager	NMB Capital Limited
Collection Centers	ASBA Approved BFIs
Min. Application (Kitta)	50
Max. Application (Kitta)	900
ICRA Rating	Not Applicable

Note: As per regulation 3 (ka) of Credit Rating Regulation, 2068 the credit rating of this issue is not required since the issue is less than NPR Three Crores.

Capital Structure (NPR)

	Existing	Post Issue
Authorized	10,00,00,000	10,00,00,000
Issued	6,00,00,000	6,00,00,000
Paid Up	4,20,00,000	6,00,00,000
Shareholding Structure (%)		
Public	-	1,80,00,000 (30%)
Promoter	4,20,00,000 (100%)	4,20,00,000 (70%)

Operational Coverage

Numbers of Authorized Districts	3
Number of Branches	8

Future Plan and Strategy

- Prioritize the branch extensions
- Increase deposit and loan amount as required
- Increase the number of its members
- Offer services and facilities as required by its members

Board of Directors

- 1) Mr. Madan Gopal Shrestha, Chairman
- 2) Mr. Udayswar Shrestha, Director
- 3) Mr. Kumar Raj Joshi, Director
- 4) Mr. Sukuman Dangol, Director
- 5) Mr. Durga Prasad Malla, Director

Management Team

- 1) **Mr. Shiva Kumar Malla, CEO**
 - Over 28 years of experience in Nepal Bank Limited as Senior Manager.
 - Over collective 10 years of experience in development banks and finance companies.
- 2) **Mr. Pratap Koirala, Assistant Manager**
 - 10 years of experiences at administrative position in Deprosc Laghubitta Bikas Bank.
- 3) **Mr. Duryodhan Malla, Assistant Manager**
 - 8 years of experiences at administrative position in Deprosc Laghubitta Bikas Bank.
- 4) **Mr. Rakesh Shrestha, Officer**
 - Working in this company for last 3 years.

Composition of Board of Directors

As per Article 27(2) of the Company, the Board shall constitute 5 members as follows:

Representing Promoters	3 members
Representing Ordinary Shareholders	1 members
Independent Director	1 member

The tenure of directors shall be 4 years.

Article 28 requires the directors representing the ordinary shareholders to hold at least 100 ordinary shares of the company.

Meeting fee of NPR 1,000, for Chairman and directors, will be paid for attending Board Meetings.

Key Shareholder (Promoters)

Name	Shareholdings (Kitta)
Mr. Rajendra Malla	31,454
Mr. Rajan Karmacharya	38,000
Ms. Indra Maya Gopaju	30,500

Market Average as per Q2 2074/75

Sector	Microfinance
Indexes	1,760.39 (as of 11/01/2075)
Listed Microfinance	36
Market Cap (NPR '000)	101,757,399.24
EPS (NPR)	20.35
BVPS (NPR)	160.59
P/E Ratio	38.94 times
P/B Ratio	6.82 times
ROE	13.52%
ROA	1.67%
CAR	12.94%
Cost Of Funds	9.20%
NPL	0.41%
Credit Deposit Ratio	102.32%

The above fundamentals are as per 2nd Quarter, 2074/75. Harmonic Mean is used as average to nullify the effect of outliers. AMFI, SMB & UMB scripts are excluded since not listed as on date.

Key Fundamentals (FY 73/74) (NPR. In Millions)

Paid up Capital	21
Reserve and Surplus	0.92
Book Value Per Share (In NPR)	103.97
Earnings Per Share (In NPR)	19.02

General Introduction to Balance Sheet Figures

Paid-Up Capital of the company will increase to **NPR.60 Million** after the public issue and project no further capital increment in next 3 years. The Reserve and Surplus of the company was negative till F.Y 72/73 and projected to increase at **241.62%** CAGR ahead, this increase is mainly caused as forecasted profit is capitalised. Borrowing is projected to increase at **CAGR 20%** and Deposits at **41.88%** but CAGR of Loan and Advances is only **32.56%**. Similarly, Cash in Hand and at Bank is projected to grow at **5%**. Total Assets of the company are projected to grow at **CAGR 28.35%**.

Comparison with Industry Figures

- BVPS of company stands out at **NPR. 102.64**, whereas industry BVPS is at **NPR. 160.59**. The company's BVPS is comparatively very less than industry average.
- The average industry CD Ratio is **102.32%**, while the company CD Ratio is **112.72%**. This shows that there is utilization of funds to loans and advances from Equity Capital.
- Company annualised **ROE 0.06%**, whereas industry average is **13.52%**. Company is not producing enough profit to the shareholders, where its peers are giving better returns.
- The company's annualised ROA is **0.009%**. When compared to industry average, it is very less because industry average is **1.67%**.

(Harmonic mean is used to measure average. AMFI, SMB and UMB are excluded. Industry average is as of Q2 74/75)

Excerpts from Balance Sheet (NPR. In Millions)

Particular	Audited		Projected		
	72/73	73/74	74/75	75/76	76/77
Paid-Up capital	15.16	21	60	60	60
Reserve/ Surplus	(3.07)	0.93	9.10	22.61	36.92
Net Worth	12.09	21.93	69.10	82.61	96.92
Borrowing	68.76	166.4	199.73	239.68	287.61
Deposits	9.45	24.73	42.03	58.85	70.62
Cash and Bank Bal.	1.09	0.67	0.71	0.94	0.99
Loans/ Advances	80.42	177.89	276.61	345.38	414.38
Total Assets	92.20	218.18	316.49	387.05	461.35

Ratios

Particular	Audited		Projected		
	72/73	73/74	74/75	75/76	76/77
BVPS (NPR)	69.02	103.97	115.01	137.53	161.53
Return on Net worth	(9.65)%	18.22%	11.42%	16.35%	14.76%
CD Ratio	102.82 %	93.05%	114.33 %	115.70 %	115.68 %
Borrowing Growth	2475%	142.06 %	20.00%	20.00%	20.00%
Advance Growth	859.55 %	121.20 %	55.38%	24.95%	19.98%
Deposit Growth	656.85 %	161.57 %	70.00%	40.00%	20.00%
Capital Fund			24.76%	23.92%	23.50%

General Introduction to Income Statement

Company is operating in profits from F.Y 72/73 and has projected to increase at **CAGR 52.97%** in the projected period. Interest income is projected to grow at **37.71%** while interest expense grows at **27.12%**. This shows better earnings. Operating expense is projected to increase at **CAGR 39%** but the CAGR of operating income is only **38.78%**, which necessitate the minimization of operating expenses. Company projects to maintain provision on total gross loan at an average of **0.7%** which needs to be adjusted according to the riskiness of the loan disbursed. The effective tax rate of the company is **27%**.

Comparison with Industry Figures

- The annualised EPS of the company is **NPR. 0.07** which is way lower than the industry average of NPR. 20.35.
- The ratio of Operating Expenses to Net Interest Income of the company is **112%** which is higher than the current industry average of **72%**. Major profit of the company is absorbed by operating expenses.
- Interest rate spread of the company is projected to be maintained at an average **10.83%**, whereas the average market IRS **6.34%**. Higher spread contributes higher revenues of the company.
- The company requires having effective policies to manage and minimize the operating expenses.

(Harmonic mean is used to measure average. AMFI, SMB and UMB are excluded. Industry average is as of Q2 74/75)

Excerpts from Income Statement (NPR in Millions)

Particulars	Audited			Projected	
	72/73	73/74	74/75	75/76	76/77
Interest Income	3.95	22.83	34.73	46.71	59.63
Interest Expenses	2.01	10.88	18.31	18.15	22.34
Net Int. Income	1.94	11.96	16.41	28.55	37.29
Operating Exp.	4.71	9.538	15.69	20.28	25.36
Provision for losses	0.95	8.71	1.10	0.82	0.84
Operating Profit	(1.81)	(1.09)	7.03	15.60	19.66
Net Profit	(1.17)	4.00	7.89	13.51	14.30

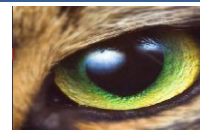
Ratios

Particulars	Audited			Projected	
	72/73	73/74	74/75	75/76	76/77
Net Int. Margin	2.21%	5.67%	5.32%	7.55%	8.25%
Net Profit Margin	(29.5%)	17.50%	22.72%	28.93%	23.99%
Op. Profit Margin	(45.7%)	(4.77%)	20.24%	33.40%	32.97%
Op. Profit Growth				122%	26%
Op. Exp. Growth	107.40 %	102.51%	64.58%	29.25%	25.00%
Cost to income ratio	122.12 %	55.59%	65.88%	55.27%	55.30%
IRS			12%	11%	9.5%
ROE %	(7.70%)	19.03 %	13.15%	22.52%	23.84%
ROA %	(1.3%)	1.83%	2.493%	3.49%	3.10%
EPS	(11.12)	19.03	13.15	22.52	23.84

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Valuation of Company

Keeping a watchful eye
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Relative Valuation Model: The idea underlying relative valuation is that similar assets should sell at similar prices. The application of relative valuation is called the method of comparable. It estimates an asset's value relative to that of another asset (benchmark). The model helps to check whether a particular stocks is overvalued, undervalued or fairly valued in terms of measures like earnings, book value, cash flow, sales per shares by comparing the industry multiples. Here, we value the company based on P/E and P/B based multiples.

P/E Ratio shows the amount investors are willing to pay for each rupee earnings of the company.

P/B Ratio shows the amount investors are willing to pay for each rupee of company *tangible* assets.

Guideline Public Company Methods: The value is based on the multiples of comparable public companies, where multiples are adjusted to reflect differences in the relative risk and growth prospects.

We assume the following:

- Discount for lack of control – Nil; since the company is a public company.
- Discount for lack of marketability – Nil; since the issue will be publicly listed in index.
- Discount for risk – Nil; since the issue is IPO and issued at par hence considered riskless

The values derived under three methods are different especially the value of FY 2074/75. The computations are made on different premises and assumptions, so it should be intuitive. Under GPCM, the value does not incorporate all the principles and using EBIT instead of EBITDA is the major constraint.

The values as computed are fair value while the market value after listing of script can significantly deviate. It has been observed that the market values of the securities are trading at relatively higher prices in the secondary market.

The computed value of Nepal Seva Laghubitta Bittiya Sanstha Ltd. is competitively good and we expect the floor price of the script to be the like.

P/B Based Valuation

Projected Year	Industry P/B (As of 2 nd Qtr)	BVPS (NPR)	Value of Shares (NPR)
2074/75	6.82	115.01	784.37
2075/76	6.82	137.53	937.95
2076/77	6.82	161.53	1,101.63

P/E Based Valuation

Projected Year	Industry P/E (As of 2 nd Qtr)	EPS (NPR)	Value of Shares (NPR)
2074/75	38.94	13.15	512.06
2075/76	38.94	22.53	877.32
2076/77	38.94	23.84	928.33

The Industry P/E and P/B as of 2nd Quarter, 2074/75 has been used since the 3rd Quarter Report of all the Microfinance Companies are not yet published.

Harmonic Mean is used to nullify the effect of outliers.

AMFI, SMB & UMB scripts are excluded since not listed as on date.

We assume Industry Average to be same.

GPCM Valuation (NPR in '000)

	74/75	75/76	76/77
EBITDA	7,028.00	15,601.00	19,661.00
Multipliers	38.28		
Enterprise Value	269,017.69	597,174.88	752,583.51
Market Value	69,996.69	358,434.88	465,956.51
Per Share MV (NPR)	116.66	597.39	776.59

Note: The industry multiple is the ratio of Enterprise Value and EBITDA as of 2nd Quarter End, 74/75.

Market Price is as of the 2nd Quarter End, 2074/75.

Operating Profit is taken as EBITDA due to inadequate financial figures for exact computation.

Debt is taken zero for all (no issuance of bond/debentures).

Strength – Weakness – Opportunities – Threat (SWOT) Analysis

STRENGTHS

- 1) As the company works in only 3 districts with limited members, company has smaller field base relationship which would be easier to control by the present human resource.
- 2) All present members are ladies which count as major strength as there is better assurance of repayment of loans.
- 3) It relies on both deposit and bank borrowings implying a diversified fund.

WEAKNESSES

- 1) Relatively low capital base of the company might cost the business opportunities of the company including the branch extension strategy, which could affect the profitability of the company.
- 2) Through the observation of the financial statements of the company, the company seems to be weak in management of staff expenses.

OPPORTUNITIES

- 1) There is always an opportunities for the company to reach its services to the greater number of customers and members, since the services are targeted to the underprivileged and poor section of the community and Nepal has still quarter of its population under poverty zone.
- 2) Besides, the company can reach to the areas where Bank cannot reach.
- 3) Since the poverty alleviation is the government major priority, the policies favouring the microfinance sectors can be expected always.

THREATS

- 1) Problems in banking sectors like liquidity problems could affect the function of the company along with intense competition among MFIs to find the business.
- 2) As the paid up capital is comparatively lower than the industry average, in case there is a regulatory requirement of increment of paid up capital, the company may be forced to be a part of merger/acquisition with an established industry player trading below its own Trading Price (As generally perceived, Micro Finance Companies with recent IPO and lower paid up capital trades at a higher end than already established industry players) and at a unfavourable swap ratio.

Tentative Allotment Module

Chapter 5, Article 30 of Securities Issue and Allotment Guidelines 2074 provides the new process of allotment of securities under which every valid applicant shall be allotted 10 kitta shares on the very first round of allotment and the round following then, provided the kittas available are sufficient for allotment to each eligible applicant. Otherwise, the lottery system will be followed.

On top right is the issue and applicants details of IPO of Arambha Microfinance Bittiya Sanstha Limited as per new process. The IPO was oversubscribed by more than 43+ times where the average kitta applied by total applicants was 63.85 units.

We estimate the IPO of Nepal Seva Laghubitta Bittiya Sanstha Ltd. will be subscribed by nearly 200,000 valid applicants and the average kitta applied is 50 units. So, the oversubscription is likely to be more than 59.73 times.

The Implementation of C-ASBA has brought revolution in the allotment of IPO. Arambha Microfinance IPO has been allotted within 36 hours by CDSC and issue manager with the help of C-ASBA system.

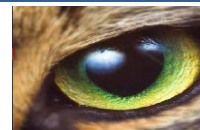
Investors are found to be more attracted in the primary market like IPOs. Almost all the IPO shares have been oversubscribed in the past. The waiting for the IPO of Microfinance sector is forefront. This is because the Microfinances are able to make good returns and the average trading prices of the Microfinances scripts are comparatively higher than other sectors scripts.

For our forecast of 200,000 valid applicants, the number of kittas required to satisfy all with minimum 10 kittas is 2,000,000. However, the company can only satisfy 16,740 applicants with 10 kitta shares. Therefore, the IPO of the company is most likely to be allotted on lottery basis where approx. 8 out of 100 applicants will get the 10 kittas share.

Arambha Microfinance Bittiya Sanstha Limited	
Issue Size (Kitta)	294,000
Staff (Kitta)	8,820
Mutual Funds (Kitta)	14,700
Public (Kitta)	270,480
Allotment Date	11/23/2074
Number of Total Applicants	186,038
Number of Valid Applicants	185,653
Application Range	50 – 1,000 units
Total Kitta Applied	11,878,750
Oversubscription	43+ times
Number of Allottees	27,048
Kittas Allotted	270,480
Allotment Basis	Lottery

Nepal Seva Laghubitta Bittiya Sanstha Limited	
Issue Units to Public	167,400
Estimated Number of Applicants	200,000
Estimated Applied Kittas	10,000,000
Oversubscription	59.73 times
Allotment	
Required Kittas	2,000,000
Available Kittas	167,400
Allotment Basis	Lottery
Number of Allottees	16,740
% Allotment	8.37%
Estimated Allotment Date	1 Week
Estimated Listing Date	15 days of Allotment
Estimated Trading Date	7 days of Listing

Though, it would be prudent to apply for minimum 50 units share but the probability of allotment on lottery is found higher for applicants applying for higher units of share.



Industry Overview and Competitiveness

The basic objective of Microfinance Institutions (MFIs) is to provide the financial services like micro-credit, savings, micro-insurance, remittance etc. to the deprived section of the community and uplift the standard of living. MFIs have a huge role and potential in a country like Nepal where a high percentage of population are deprived socially and economically. Microfinance programmes are established and promoted in Nepal with diversified method and modalities like Grameen Banking Model, Deprived Sector Lending Model, Saving and Credit Co-operative Model, Wholesale Lending Model etc.

To carry out the objective, MFIs borrow the money from other BFIs at cheaper rates and lend it to the needed people. Nepal Rastra Bank has classified Microfinance as Class “D” Financial Institution.

MFIs have huge prospects in Nepal since it can serve and extend its services to the wide range of low income people. It has been making good profits which can be reflected in the higher trading prices of its shares. Although returns are contributed by the micro lending of the institutions, it has been able to extend services to remittances, insurances etc.

On the other hand, microfinance can be subject to many risk factors. Major can be the Interest rate change risk, credit risk, operational risk etc. Also, the state of overall Banking and Financial Industry also impact the performance and functioning of the Microfinance Institutions.

Despite the government appeal and direction, MFIs has not been able to reach its services to the weaker sections as it should have been, due to many obstacles like poor infrastructure, geographical difficulty, no financial awareness and ideas and initiatives among the people.

Current Situation of MFIs	
Listed MFIs	36
Registered MFIs	48
National Level	21
1 District	1
1-3 District	2
4-10 Districts	20
10+5 District	4

Listing of Shares of Nepal Seva Laghubitta Bittiya Sanstha Limited

The book value per share of the company as of FY 2073/74 is Rs.103.97. Therefore, the listing price of the share should be in the range of Rs.103.97 (lower range) and three times of lower range i.e. Rs.311.91 (upper range).

Trading Prices

The share can be expected to trade at relatively higher prices. The listed shares of the company are comparatively lower due to which supply will be low and demand will be higher. There will be 180,000 shares of the company floating in the market and company has no projection of increasing the capital in the coming period. However, the promoter's shares i.e. to the extent of 420,000 units can be expected to float in the market after 3 years from allotment date of the public issue. This could affect the pricing of the shares in the secondary market.

Technical Analysis

Microfinance Index is Trending Higher



A separate microfinance index data was available only from November 2017 and for that reason a 10-minute chart is used here. Microfinance index has surged since April 2018. During the last week of March, microfinance sub index was around 1220 region. Whereas as of now (April 23), it is in the 1770 region, it is a 45% rise within a month. The uptrend has formed at an accelerating rate which is also confirmed by the rising volume which is an indication of a sustainable market trend.

Microfinance index is below the 5-day and 20-day simple moving averages which indicate market is in correction phase at the moment. However, recently index has bounced from the lower band which suggests struggle to rise. Average true range (ATR) has been in a rising trend which means the volatility has increased. The negative directional movement index (-DI) is above the Positive (+DI) showing a negative trend at the moment. The general trend of on balance volume (OBV) has been up signalling increased volume with the price. On the daily chart stochastic is in the oversold territory.

This sector may face a short term correction in near future which may take the sub index to 1600 levels. A bounce from aforementioned level will be an accumulating opportunity.

RECOMMENDATION: APPLY

The IPO of Nepal Seva Laghubitta Sanstha is ideal to **APPLY** by the investors. The company has been able to make profit positive in the short period of operation. However, the projected statements provides growth but at a slower pace which could question the competitiveness of the company in the microfinance industry. It is important for the company to manage the expenses figures to increase the profitability. Since, the company projects no further capital increment upto FY 2076/77 after the public issue, the company may not provide any bonus or right shares. The company may retain significant portion of revenues for branch extension and other projects and thus provide small margin of cash dividend. The valuation as performed provides the reasonable intrinsic values and the trading prices in the secondary markets can be expected to be well above these values. The company is managed by experienced personnel having years of contribution in the Microfinance industry. Beside the basic nature of functions of Microfinances, the company is also providing other services like remittance to the general public, adding revenue sources of the company. Nevertheless, the investment of Rs.100 in the IPO of the Microfinance are certain to be of 'no regret' but best investment since they are providing benefits in the form of dividends (cash/bonus) and rights while the secondary market prices are very lucrative which are certain to cover any cost (implicit/explicit). *The investors are recommended to apply for a minimum kitta because the allotment is highly to be on lottery basis.*

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