

**Rating Rationale**  
**Samaj Laghubitta Bittiya Sanstha Limited**

**Rating**

Particulars	Amount	Rating <sup>1</sup>	Rating Action
Issuer Rating	NA	CARE-NP B+ (Is) [Single B Plus (Issuer)]	Assigned

CARE Ratings Nepal Limited (CRNL) has assigned ‘CARE-NP B+ (Is)’ rating to Samaj Laghubitta Bittiya Sanstha Limited (SLBS). Issuers with this rating are considered to offer high risk of default regarding timely servicing of financial obligations, in Nepal.

**Detailed Rationale & Key Rating Drivers**

The Issuer Rating assigned to SLBS is constrained by lower level of capitalization against minimum requirement, weak financial performance marked by net loss during FY19 (Audited; refers to the 12 months period ended Mid-July 2019) and 9MFY20 (Unaudited; refers to the 9 months period ended Mid-April 2020) alongwith short track record and small scale of operation with limited geographical coverage. The rating is also constrained by SLBS’s high dependence of resource profile on Banks & Financial Institutions (BFIs) borrowings, competition from other Micro Finance Institutions (MFIs) and Co-operatives and inherent risk involved in the microfinance industry. The rating, however, derives strength from experienced board members and management team, growth in loans and advances and deposits during 9MFY20, moderate liquidity profile, good assets quality and diversified sector wise credit portfolio distribution. Ability of the company to continue its growth momentum without compromising on asset quality and maintaining the Capital Adequacy Ratio would be key rating sensitivity.

***Impact of Covid-19 in the business***

The outbreak of Coronavirus disease 2019 (COVID-19) which was recognized as Pandemic by World Health Organization has affected Nepal as well. Government of Nepal (GoN) countrywide lockdown since March 24, 2020 closing most of the organizations which resulted in slowing down of the economic activities. MFIs lend to members belonging to low income groups and collection of due amounts are made in cash. Due to lockdown imposed, MFIs has been impacted as they were not able to collect the due amounts from borrowers. Nepal Rastra Bank vide Monetary Policy for FY20-21 has directed MFIs to provide maximum 6 months of moratorium for loans due by Mid July 2020. SLBS has accordingly rescheduled few loans based on case to case basis for few months.

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com)

## Detailed Description of the Key Rating Drivers

### Key Rating Weakness

#### *Lower level of capitalization against minimum requirement*

SLBS's overall Capital Adequacy Ratio (CAR) stood at 15.55% in FY19 in comparison to the minimum regulatory requirement of 8% for microfinance institutions (MFIs). However, company reported overall CAR of 5.39% during 9MFY20 due to increase in risk weighted assets (RWA) on the back of increase in loans and advances by ~198% during 9MFY20.

#### *Weak financial performance marked by net loss during FY19 and 9MFY20*

SLBS started operation from April 15, 2018 and had its first full year of operation only during FY20. During FY19, SLBS reported interest income of Rs. 3.99 Mn and total income of Rs. 5.19 Mn. Further, net interest income during FY19 was Rs. 1.65 Mn with company reporting net loss of Rs. 2.13 Mn due to higher operating cost as compared to income.

During 9MFY20, company reported interest income of Rs. 10.65 Mn on the back of increased loans and advances during the period whereas net interest income was Rs. 2.85 Mn. Interest cost increased to Rs. 7.80 Mn due to increase in loans availed by the company. Further, the company reported total income of Rs. 14.57 Mn during 9MFY20 due to increase in interest income and other operational income (includes service charges and renewal fees). Operational expenses increased to Rs. 6.25 Mn during 9MFY20 and company reported net loss of Rs. 0.51 Mn. Its operating expenses/ average total assets improved to 7.18% in 9MFY20 from 13.78% in FY19 due to increase in total assets was higher than operating expenses. Net Interest Margin (NIM) ratio decreased to 3.28% in 9MFY20 from 5.01% in FY19 on the back of higher increase in total assets as compared to increase in net interest.

#### *High dependence of resource profile on Banks & Financial Institutions (BFIs) borrowings*

SLBS's major source of funding consist of borrowing from BFIs. The ratio of borrowing from BFIs to total resource was high at ~78% in 9MFY20 which increased from ~74% in FY19. As on April 12, 2020, its funding is tied up with 6 BFIs. Due to use of large portion of debt, its cost of fund was high (i.e. 10.34% in 9MFY20) which put pressure on profitability.

#### *Short track record of operation with limited geographical coverage*

SLBS has short track of operation as it is operating since April 15, 2018 and had its first full year operation only in FY19. Further, SLBS has license for operation in only 3 districts. As on Mid-April 2020, SLBS has 5 branches covering 3 districts within Province 2 of Nepal.

#### *Competition from other MFIs and Co-operatives*

As on Mid-April 2020, there were 89 MFIs in operation with total 3,942 branches all over Nepal. SLBS has 5 branches as on Mid April, 2020. Micro Finance Industry earned Rs. 29,482 Mn interest income, Rs 13,255 Mn net interest income and Rs 4,824 Mn Net profit during 9MFY20. SLBS reported Rs. 10.65 Mn interest income and Rs. 2.85 Mn net interest income for the same period in the industry depicting a low share in the market. Further, large number of cooperatives are operating all over Nepal which provides

loans and other financial services to their members with or without collateral. Due to presence of large number of micro finance and co-operatives, SLBS is facing competition to tap the new customer.

#### ***Inherent risk involved in the microfinance industry***

MFIs are prone to credit risk which is directly related to the portfolio of the organization and is one of the most significant risks from MFI's perspective. Credit risk assumed by a MFI is typically higher compared to banks and other types of lenders given the weak borrower profile. Further, MFIs provide unsecured loan i.e. loan without any collateral. In case any borrower defaults, the MFI does not have any assets backed as collateral to meet its loss, which makes the credit even riskier. As borrowing from MFIs do not require collateral, clients tends to borrow from multiple MFIs resulting to problem of loan duplication. Absence of credit report from Credit Information Bureau (CIB) is one of the reasons for loan duplication. However, monetary policy of 2018-19 required MFIs to send credit information to CIB continuously and failing to comply the same will result in 2% additional Loan Loss Provision (LLP). As per NRB norms, MFIs are allowed to lend against collateral upto 33.33% of total lending. SLBS's loan portfolio consisted 100% loan without collateral during 9MFY20.

#### **Key Rating Strengths**

##### ***Experienced board members and management team***

SLBS has 5 members on its board. The board is chaired by Mr. Dilip Kumar Dhaumdel, who has long experience in banking sector with 27 years of experience in Agriculture Development Bank Limited (ADBL). He is also promoter of the company with 1.75% holding as on Mid-April 2020. Other directors of the company have long track record of banking experience. The company's management team is led by Chief Executive Officer, Mr. Kishori Mahato, who has more than 2 decades of experience in banking sector and has worked in ADBL for 28 years. He is supported by other experienced management team.

##### ***Moderate Liquidity Profile***

SLBS has moderate liquidity profile with positive cumulative mismatch over one year as on April 12, 2020 due to well mismatch tenure of assets and liabilities. However, due to deferment of loan amount and any delay in recovery of due amount due to COVID-19 would be critical for liquidity. SLBS has maintained CRR 0.63% in FY19 which is in compliance with NRB norms. SLBS maintained 0.49% in 9MFY20 which was below minimum requirement. However, SLBS has maintained CRR above minimum requirement during Mid June 2020.

##### ***Growth in loans and advances and deposits during 9MFY20***

SLBS's credit portfolio grew by ~198% to Rs. 151 Mn at the end of 9MFY20 from Rs 51 Mn in FY19 due to increase in member base (2,150 members in FY19 to 4,584 in 9MFY20).

##### ***Good assets quality***

SLBS's NPL level was Nil at the end of FY19 and 9MFY20 mainly due to new loans, strict credit policy and regular follow-up. It's ability to maintain low level of NPL in long term is challenging as loan duplication problem is major issue in microfinance industry.

***Diversified sector wise credit portfolio distribution***

SLBS has been disbursing loans to various sectors such as agriculture sector which includes animal husbandry, poultry, vegetable, fishery, bee keeping, fruits and flower etc., small and cottage industry, service industry which includes wholesale and retail business, hotel and restaurants, and others. During 9MFY20, it has lent 51.32% (41.06% in FY19) towards Agriculture followed by 42.81% (45.40% in FY19) towards service industry.

**About the Company**

Samaj Laghubitta Bittiya Sanstha Ltd. (SLBS) is a “D” class microfinance institution incorporated on May 3, 2017, licensed by Nepal Rastra Bank on April 15, 2018 for operating in 3 districts of Nepal. It is promoted by individuals from different background and is primarily engaged in providing microfinance loan based on the Joint Liability Group (JLG) model with each group consisting of five members. As on Mid April, 2020, it has total paid up capital of Rs. 11.40 Mn. Company is planning to issue IPO of Rs. 8.60 Mn. After issue of proposed IPO, the share capital of the company will be Rs 20 Mn which will be held by promoter and public shareholders in 57:43 ratio.

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