

Unique Nepal Laghubitta Bittiya Sanstha Limited

Ratings

Facilities	Amount (Rs. in Million)	Rating ¹	Rating Action
Issuer Rating	NA	CARE-NP BB- (Is) [Double B Minus (Issuer)]	Reaffirmed

CARE Ratings Nepal Limited (CRNL) has reaffirmed the issuer rating of "CARE-NP BB- (Is) [Double B Minus (Issuer)]" assigned to Unique Nepal Laghubitta Bittiya Sanstha Limited (UNLBSL). Issuers with this rating are considered to offer moderate risk of default regarding timely servicing of financial obligations in Nepal.

Detailed Rationale & Key Rating Drivers

The ratings assigned to UNLBSL continues to be constrained by its weak asset quality profile, competition from other Micro Finance Institutions (MFIs) and Co-operatives and inherent risk involved in the microfinance industry. The rating is also constrained by exposure to regulatory risks related to microfinance industry. The rating, however, derives strength from backup of strong institutional promoter, experienced board members and management team and long track record of operations. The rating also factors in moderate liquidity profile and improved financial performance leading to increased capital cushion over minimum regulatory requirements during FY21 (audited; refers to the twelve-month period ended mid-July 2021) and H1FY22 (unaudited; refers to the six-month period ended mid-January 2022).

Going forward, the ability of the company to continue its growth momentum with improving asset quality and capital adequacy ratio and its ability to manage the impact of any regulatory changes will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Weak asset quality

UNLBSL's asset quality remains weak marked by high Gross Non-Performing Loans (GNPL) ratio. GNPL as a percentage of total loans and advances stood at 7.45% at the end of FY21, albeit improved to 4.98% as on mid Jan 2022; still remarkably higher. Primary reason for high GNPL was due to impact of the pandemic on the borrowers. Furthermore, more than 30-day delinquency of UNLBSL was also high at 29.20% of total advances as on July 15, 2021. This has reduced to 9.05% as on January 14, 2021 helped by improved recovery during H1FY22. However, given the lingering impact of the pandemic, deterioration in asset health in a short span remains a risk and hence tight monitoring of the asset quality will remain critical for the company's financial health going forward.

Competition from other MFIs and Co-operatives

As on mid-January 2022, there were 67 MFIs in operation with total of 5,046 branches in Nepal. UNLBSL had 47 branches as on mid-January, 2022. Micro Finance Industry earned Rs. 41,688 Mn interest income, Rs 10,759 Mn net interest income and Rs 10,669 Mn Net profit during FY21. UNLBSL had 1.02% (Rs. 427 Mn) share on interest income for the same period in the industry. Furthermore, large number of cooperatives are operating all over Nepal which provide loans and other financial services to their members with or without collateral. Due to presence of large number of micro finance and co-operatives, UNLBSL is facing competition to tap the new customer and to retain the existing good consumer.

¹Complete definition of the ratings assigned are available at www.careratingsnepal.com and other CARE publications

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. Furthermore, MFIs provide unsecured loan i.e. loan without any collateral. In case any borrower defaults, the MFI does not have any asset backed as collateral to meet its loss, which makes the credit even riskier. As borrowing from MFIs do not require collateral, clients tend to borrow from multiple MFIs resulting to problem of loan duplication. As per NRB norms, MFIs are allowed to lend against collateral up to 33.33% of total lending. UNLBS's percentage of collateral loan to total loan is 3.37% in FY21 and 3.12% in H1FY22 which has decreased from 3.56% in FY20.

Exposure to regulatory risks related to microfinance industry

The microfinance industry is exposed to changes in the various regulatory measures issued by NRB from time to time. As per the earlier regulations, A, B & C class financial institutions were required to extend 5%, 4.5% and 4% respectively of their total loans towards deprived sector. As per the regulations, Class A, B & C financial institutions are also required to lend 5% of their total advances to deprived sector. Monetary policy 2019/20 has capped interest rate up to 15%. Further, regulator has capped fees at 1.5%, scrapping the interest rate spread cap of 9%. As a result of this provision, MFI cannot charge interest rate more than 15% which will restrict interest earning capacity and yield from FY21 onwards.

Key Rating Strengths**Experienced board members and management team with backup from strong institutional promoter**

At the end of FY21, 65.24% of current paid up capital of UNLBSL is held by institutional promoters namely United Youth Community (UNYC Nepal), Prabhu Bank Limited (CARE-NP BBB) and Nepal Credit and Commerce Bank Limited. UNLBSL has five members on its board and is chaired by Mr. Kali Prasad Chaudhary, with more than 35 years of experience in various sectors. The company's management team is led by Executive Director Dr. Gopal Dahit, who has more than 21 years of experience in microfinance sector. He is supported by other experienced management team to look after various functions in the company.

Moderate capital cushion over minimum regulatory requirement

UNLBSL's Tier I and overall Capital Adequacy Ratio (CAR) stood at 8.64% and 9.89% respectively at the end of FY21 over the minimum regulatory requirement of 4% and 8%, respectively, for microfinance institutions (MFIs). Overall CAR marginally deteriorated to 9.80% at the end of H1FY22, which is expected to improve after issue of proposed public issuance of around Rs. 38 Mn. UNLBSL completed merger with Ghodighoda Laghubitta Bittiya Sanstha Ltd during H1FY22 which has helped increase the company's paid up capital to over Rs. 100 Mn, as required for a MFI with presence in more than one province.

Improved financial performance marked by sustained growth in advances and income in FY21

UNLBSL's credit portfolio grew by 18.94% year on year to Rs 2,979 Mn in FY21. UNLBSL has 1.59% and 1.24% market share in terms of deposit base and loan portfolio, respectively, of the microfinance industry in FY21. During FY21, UNLBSL's total income increased to Rs. 494 Mn from Rs 452 Mn during FY20. Interest income improved by 4.54% to Rs 427 Mn due to the growth in advances by 18.97% to Rs. 2,979 Mn. Consequently, net interest income increased to Rs. 242 Mn during FY21 from Rs. 193 Mn during FY20. Overall financial performance has improved backed by increasing scale of operations. Addition of new branches and the recently completed merger is likely to help continue this growth trend for UNLBSL over the medium term.

Moderate Liquidity Profile

As on July 15, 2021, UNLBSL shows moderate liquidity profile with positive cumulative mismatch over one year. The CRR of UNLBSL has been maintained at 0.53% in FY21 and 0.52% in H1FY22 against minimum requirement of 0.5%. Further, UNLBSL

has maintained net liquid asset ratio of 3.93% in H1FY21 and 6.29% in FY21 against the minimum regulatory requirement 2.5% for MFIs not taking public deposits.

About the Company

UNLBSL is a "D" class microfinance institution incorporated on August 03, 2018, licensed by Nepal Rastra Bank on November 11, 2018 and commenced operation on December 16, 2018. Thereafter, UNLBSL took over the microfinance business of UNYC, an NGO established in 1995 and operating as a financial intermediary since 2000 in Nepal. UNLBSL is primarily engaged in providing microfinance loan based on the Joint Liability Group (JLG) model with each group consisting of minimum five members.

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