

Manjushree Finance Limited

Ratings

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

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

Detailed Rationale & Key Rating Drivers

The rating assigned to MFIL continues to be constrained by its weak assets quality, low share of CASA deposits, moderate concentration over borrowers and depositors, modest liquidity profile, exposure to regulatory risk related to banking industry and intense competition. The rating is also constrained by modest financial performance during FY22 (Unaudited, refers to 12 months' period ended mid-July 2022) and decline in investment portfolio of the company.

The rating, however, continues to derive strength from the experienced board and management team, adequate capitalization levels, increasing scale of operations backed by considerable growth in advances and deposits with increasing geographical presence and diversified credit portfolio.

Going forward, the ability of the company to continue its growth momentum while 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 assets quality with significant decline in investment portfolio

MFIL has a weak asset quality profile marked by Gross Non-Performing Loans (GNPL) ratio of 2.19% of total loans and advances as on mid-July 2022 (industry average: 1.40%) compared to 2.01% as on mid-July 2021. GNPL ratio further deteriorated to 2.44% of total loans and advances as on mid-Oct 2022 with borrowers impacted by the ongoing liquidity crisis. Out of total loans of Rs. 10,623 Mn as on mid-July 2022, delinquencies (including restructured loan) of more than 30 days stood at 12.67% (Rs. 1,346 Mn) which improved from 16.85% of total advances at the end of FY21. The company's ability to maintain asset quality by managing further slippages will remain critical from credit perspective.

MFIL's fair value of investments declined to Rs. 1,874 Mn at the end of FY22 from Rs. 4,745 Mn at the end of FY21 on account of sale of bonds and treasury bills during FY22.

Moderate portfolio concentration among top borrowers and depositors

MFIL has moderate concentration on lending as top 20 borrowers accounted for 13.04% of total loans and advances at the end of FY22 which decreased from 22.15% at the end of FY21. Due to concentration over top borrowers, there may be risk on its assets quality due to increase in impact of any big borrowers' default on loan. Furthermore, MFIL's deposits from top 20 depositors remain moderate at 19.04% of total deposit in FY22 which increased from 15.35% of total deposit in FY21. Top 20 depositors mainly consist of institutional depositors. Lower concentration towards deposits normally reduces re-pricing risks at times of interest rate volatility.

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

Modest financial performance during FY22

During FY22, MFIL's total income decreased by 6.24% year-on-year to Rs. 1,526 Mn (FY21: 1,627 Mn) mainly on account of decline in non-interest income by 87.69% to Rs. 83 Mn in FY22. The higher non-interest income in FY21 was on account of MFIL reporting profits on sale of investments of Rs. 625 Mn during FY21 (FY22: Rs. 8 Mn) amid a more favorable market dynamic during FY21. MFIL's Net Interest Margin (NIM) improved to 2.90% during FY22 from 2.45% during FY21.

The total operating expenses increased by 7.56% in FY22 to Rs. 276 Mn compared to Rs. 257 Mn during FY21 on account of increase in branches coupled with increase in other operating expenses. MFIL's PAT declined by 78.19% to Rs. 108 Mn during FY22 from Rs. 497 Mn during FY21. MFIL's Return on Total Assets (ROTA) decreased to 0.73% in FY22 from 4.33% in FY21 due to decrease in PAT compared to previous year. Similarly, return on net worth (RONW) also decreased to 6.13% in FY22 from 32.28% in FY21.

Modest CASA deposit ratio and liquidity profile

MFIL's CASA mix continues to remain lower than the industry average. MFIL's CASA deposit to total deposits declined to 16.00% (lower than finance industry average of 20.79%) as on mid-July 2022 from 25.64% at the end of FY21 (finance industry average of 30.47%). CASA deposits declined by 19.94% at the end of FY22 to Rs. 1,829 Mn over FY21. Due to decrease in CASA proportion, cost of deposits has increased to 9.96% at the end of FY22 compared to 8.16% at the end of FY21. Increasing cost of the funds could impact the company's profitability in the long term, resulting in a competitive disadvantage. The ability of the company to maintain lower cost of funds will be critical as it would continue to provide a competitive advantage in the "base rate plus" lending rate regime.

MFIL has modest liquidity profile with negative cumulative mismatches till bracket of 271-365 days as of mid-July 2022. However, Net liquid assets to total deposits of MFIL stood at 28.67% as on mid-July 2022 which decreased from 39.10% as on mid-July 2021 which is in compliance with the minimum requirement of 20%.

Competition from other Finance Companies and Banks

Currently, there are 17 finance companies operating with total 267 branches all over Nepal (based on monthly statistics published by NRB for Mid-July, 2022) out of which MFIL has 26 branches. Industry (Class 'C' Banks-Finance Companies) has achieved total interest income of Rs. 11,517 Mn in FY22 with Rs. 3,450 Mn net interest incomes; MFIL's share on interest income and net interest income is 12.53% (Rs. 1,442 Mn) and 12.43% (Rs. 429 Mn) respectively for the same period. Despite being one of the leading finance company in the industry, it is challenging for MFIL to maintain current market share and expand its business, due to high competition among bank and finance companies, existence of large number of finance companies along with Commercial and Development banks conducting similar kind of businesses and they lend at lower interest rate as well as they offer wider banking services than finance companies.

Exposure to regulatory risk related to the industry

The Banking and Finance industry in Nepal is exposed to changes in the various regulatory measures issued by NRB from time to time. From FY22 end, NRB has changed to Credit to Deposit (CD) ratio mechanism from existing Credit to Core Capital plus Deposit (CCD) ratio measures. CD ratio needs to be maintained below 90% from mid-July 2022 from earlier provision of 85% for CCD. Furthermore, risk weights of certain loans including personal overdrafts, TR loans, hire purchase loans for personal purpose, margin lending, etc. has been increased to 150% from existing 100% via the mid-term review of monetary policy issued by NRB for FY22. These changes are likely to put downward pressure on capital adequacy ratios of the banks and limit their ability for significant credit expansion, at least over the near term. Furthermore, bank rate has been increased to 8.5% from 7% and repo rate increased to 7% from 5.5% in the monetary policy issued by NRB for FY23. Increased bank rates will likely put upward pressure on both lending and deposit interest rates of the bank over the near term.

Key Rating Strengths

Experienced board members and management team

Established in the year 2007, MFIL has around 15 years of operational history in Nepal. MFIL is a professionally managed company under the overall guidance of its Board of Directors (BoD) led by Chairman Mrs. Indira Pandit who has work experience in finance profession of around a decade. The company's management team is led by Mr. Narayan Subedi, Chief Executive Officer, who has more than 19 years of banking experience.

Increasing scale of operations backed by considerable growth in advances in FY22 with increasing geographical presence

The total loans and advances of MFIL grew at a compounded annual growth rate (CAGR) of 19.16% over last 4 years ending mid-July 2022. At the end of FY22, total loan portfolio stood at Rs. 10,623 Mn increasing 32.10% from Rs. 8,041 Mn at the end of FY21. The overall class C finance industry's loan portfolio grew by a CAGR of 10.76% over last 4 years ending mid July 2022 with year on year growth of 20.64% at the end of FY22. Similarly, total deposits of MFIL grew at a CAGR of 17.14% over last 4 years ending Mid July, 2022 supported by increasing network, improving product offerings and effective marketing strategy. Deposits grew by 28.34% to Rs. 11,437 Mn in FY22 from Rs. 8,912 Mn in FY21 (Class C finance industry deposit grew by CAGR of 13.24% over last 4 years ending Mid-July 2022 with year on year growth of 17.02% in FY22). As on mid-July 2022, MFIL constitute 10.94% and 12.31% of market share of the overall finance industry in terms of deposit base and loan portfolio respectively (11.07% and 11.26% respectively as on mid-July 2021), based on monthly data published by NRB.

Furthermore, MFIL is operating in 6 provinces out of 7 through its 26 branches and an extension counter as on mid-July 2022 as compared to 11 branches and an ATM terminal at the end of FY21.

Adequate capitalization level, although declining trend remains a concern

MFIL's Tier I Capital Adequacy Ratio (CAR) stood at 14.01% as on mid-July, 2022, declining from 21.37% as on mid-July 2021. However, MFIL continues to have moderate cushion over the minimum regulatory requirement of 6%. MFIL's overall CAR stood at 19.70% as on Mid July, 2022 declining from 28.99% as on mid-July 2021 as against minimum regulatory requirement of 10%. The decline in CAR at the end of FY22 was also, in part, on account of NRB increasing risk weights of some loan categories such as certain personal loans, real estate loans, hire-purchase loans etc. to 150% from 100%. This had added to the increase in Risk Weighted Exposure (RWE) of the company at the end of FY22 by 19.42% over PY. However, the overall CAR remains higher than the other Class- C finance companies in the industry (average industry CAR was 15.64% based on monthly report of Mid July, 2022 published by NRB). The company's ability to maintain adequate cushion in the capital adequacy ratios is critical for its solvency and will remain crucial for its growth perspective.

Diversified credit portfolio

MFIL has a diversified portfolio distribution which consists of various types of loans disbursed over the period for various industry/sector with higher lending of 39.33% of total advances towards consumption loans followed by 21.09% towards finance, retail and insurance sector. As on mid-July 2022, MFIL lent 18.17% of gross loans and advances outstanding prior to 6 months towards productive sector (which includes agriculture sector, energy sector, tourism sector and cottage and small industries). Diversification helps bank to maintain the bank's assets quality and mitigate volatility risk in case of experienced swings in the economy.

About the Company

Manjushree Finance Limited (MFIL) is a national level class "C" finance company incorporated June 20, 2007 as Manjushree Financial Institution Ltd which was changed to Manjushree Finance Ltd. on September 2, 2016. It commenced its operations on October 15, 2007. At the end of FY22, MFIL has Rs. 1,352 Mn paid up capital which is distributed among promoters and public shareholders in the ratio of 51:49.

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