Aatmanirbhar Laghubitta Bittiya Sanstha Limited

Rating

Facilities	Amount (Rs. in Million)	Rating[1]	Rating Action
Issuer Rating	**NA**	**CARE-NP B+ (Is) [Single B Plus (Issuer)]**	**Assigned**

CARE Ratings Nepal Limited (CRNL) has assigned rating of 'CARE-NP B+ (Is)' [Single B Plus (Issuer)] to Aatmanirbhar Laghubitta Bittiya Sanstha Limited (ALBSL). Issuers with this rating are considered to have high risk of default regarding timely servicing of financial obligations.

Detailed Rationale & Key Rating Drivers

The rating assigned to ALBSL is constrained by its small scale of operations with short track record of operations, weak asset quality, and high dependence on Banks and Financial Institution (BFIs) borrowings. The rating also factors in the inherent risk involved in the microfinance industry, exposure to regulatory risks related to microfinance industry and competition from other Micro Finance Institutions (MFIs) and Co-operatives. The rating, however, derives strength from ALBSL's experienced board members and management team, improving financial profile, moderate liquidity profile, and improving capitalization levels with moderate cushion over minimum regulatory requirements at the end of 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 without compromising on asset quality and maintaining the 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, although improving trend in H1FY22

ALBSL's asset quality is weak marked by high Gross Non-Performing Loans (GNPL) ratio of 5.07% of total loans and advances as on mid- July 2021. Although this improved to 4.18% as on mid-January 2022 aided by accelerated recoveries, it is still remarkably higher than the industry average of 2.08%. More than 30-day delinquency of ALBSL, however, remained manageable at 6.95% of total advances as on July 15, 2021 and decreased to 6.03% as on mid-January 2022. Given the lingering impact of the pandemic, exacerbated by the ongoing liquidity crisis deterioration in asset quality 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.

Short track record of operation with small scale

ALBSL has been operational since April 15, 2019 and has 22 branches covering four districts (out of 77 districts) as on mid-January 2022. Being a province level microfinance company, ALBSL's scope for growth are, at least for now, limited to a single province. Due to geographically concentrated business, the customer base and portfolio of the bank is relatively less diversified which increases the risk of volatility of a single economic region.

Increasing dependence on Banks & Financial Institutions borrowings

ALBSL's major source of funding consists of deposits from its members and borrowings from banks and financial institutions (BFIs). The ratio of borrowing from BFIs to total resource decreased to 18.91% in FY21 from 24.90% in FY20, which resulted in

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

decrease in average cost of borrowings to 7.02% in FY21 from 9.88% in FY20. Higher reliance on BFIs increases the MFI's cost of fund and is likely to squeeze spread leading to lower profitability.

Competition from other MFIs and Co-operatives

As on mid-January 2022, there were 67 MFIs in operations with total of more than 5,000 branches in Nepal. ALBSL had 22 branches as on mid-January, 2022. Micro Finance Industry earned Rs. 45,304 Mn interest income, Rs 27,025 Mn net interest income and Rs 11,829 Mn Net profit as on Mid-July 2021. ALBSL has 0.42% (Rs. 189 Mn) share on interest income for the same period in the industry. Further, large numbers of cooperatives (National and Provincial level) 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, ALBSL is facing competition to tap the new customer and to retain the existing consumers.

Inherent risk involved in the microfinance industry

Micro Finance Institutions 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 MFI is typically higher compared to banks and other types of lenders given the weak borrower profile. Furthermore, majority of MFI's loan portfolio is unsecured in nature means advances not secured by adequate 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 borrowings from MFIs do not usually 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. ALBSL's percentage of collateral loan is 16.29% of total lending in FY21 and 20.38% in H1FY22 which has increased from 9.01% in FY20.

Key Rating Strengths

Moderate capitalization levels

As on mid-July 2021, the Tier I capital ratio and overall Capital Adequacy Ratio (CAR) of ALBSL stood at 11.43% and 12.67% respectively against the minimum regulatory requirement of 4% and 8%, respectively, for microfinance institutions (MFIs). Overall CAR increased further to 13.59% as on mid-January 2022 aided mainly by profit accretion to reserves. The total paid up capital of the company is Rs 42 Mn as on mid-January 2022. As per new Unified directives 2020 issued by NRB, the company operating as a regional level MFI shall have minimum paid up capital of Rs. 60 Mn within 3 years from the commencement of commercial operation. ALBSL expects to meet this requirement through public issuance of Rs. 20.34 Mn latest by second half of FY23. This will remain a key monitorable aspect.

Backup from experienced institutional promoter

As on mid-January 2022, 64.29% of paid up capital of ALBSL was held by institutional promoter namely Gramin Mahila Utthan Kendra (GMUK**)**. GMUK is a registered NGO, established in the year 1993 to promote the indigenous society and unite to combat for gender equality, justice and dignity. GMUK has been conducting microfinance program to uplift the poor and deprived families in Dang. The institution has serviced more than 20,000 families with microfinance services. ALBSL can tap on the established reach of its promoter GMUK to help expand its customer base.

Financial risk profile marked by growth in revenue and profitability with moderate liquidity

ALBSL's credit portfolio grew 29.55% year on year (yoy) to Rs 1,182 Mn at the end of FY21. During H1FY22, credit portfolio grew by 16.26% over FY21 to Rs 1,374 Mn. ALBSL had 0.61% and 0.32% market share in terms of deposit base and loan portfolio, respectively, of the microfinance industry at the end of FY21. During FY21, ALBSL's interest income increased by 8.07% yoy to Rs 189 Mn due to the growth in advances by 29.55% to Rs 1,182 Mn. Consequently, ALBSL's Net Interest Margin improved to 9.86% in FY21 from 8.05% in FY20. Overall financial performance has improved backed by growth in scale of operations. Furthermore, ALBSL has a moderate liquidity profile as indicated by CRR maintained at 0.53% against minimum requirement of 0.5% and net liquid asset ratio of 9.77% against the minimum regulatory requirement 2.5% for MFIs not taking public deposits as on mid-January 2022.

About the Company

ALBSL is a “D” class Province Level microfinance institution. It was incorporated on November 20, 2018, licensed by Nepal Rastra Bank on February 12, 2019 and commenced operations on April 15, 2019. Initially, ALBSL commenced its business as Gramin Mahila Utthan Kendra (Rural Women Development Center-RWDC), a financial intermediary. However, of lately, ALBSL initiated its operation as a separate financial entity. ALBSL 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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Our parent company, CARE Ratings Limited commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI).