

Sunrise Capital Limited

Ratings

Facilities	Amount (Rs. Million)	Rating ¹	Rating Action
Fund Management Quality Rating (FMQR)	NA	CARE-NP AMC Quality 3 (AMC 3)	Reaffirmed

The explanatory notes regarding the scale and definitions for FMQR of CARE Ratings Nepal Limited (CRNL) are attached as Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the Fund Management Quality Rating (FMQR) of 'CARE-NP AMC Quality 3 (AMC 3)' assigned to Sunrise Capital Limited (SCL). CARE-NP AMC Quality 3 (AMC 3) indicates adequate assurance on management quality of Asset Management Company (AMC).

Detailed Rationale & Key Rating Drivers

The rating assigned to SCL continues to derive strength from its strong fund sponsor/ shareholders, experienced board of directors and management team in merchant banking and overall banking services, and SCL's established track record of operations in merchant banking. The rating also factors in professional fund supervisors, diversified investment portfolio, improving merchant banking performance over the period and past experience in handling Mutual Fund Schemes.

The FMQR, however, is constrained on account of evolving nature of industry, volatile investment income, volatile trend of Nepal Stock Exchange (NEPSE) index and limited market diversification in the industry.

Detailed description of the key rating drivers

Key Rating Strengths

Strong fund sponsor/ shareholders, and established track record of operations in merchant banking

SCL have been providing merchant banking services from the last two decades. The company was previously known as NIDC Capital Markets Limited (NCML) and was established on January 26, 1993 to carry on financial services and merchant banking services in Nepal. The company is a wholly owned subsidiary of Sunrise Bank Limited (SBL; rated CARE NP A- (Is)), an "A" Class Licensed Institutions from Nepal Rastra Bank (NRB). SCL avails technical and management support from its parent company SBL. SCL is utilizing the existing branch network of SBL to provide the merchant banking services like opening demat accounts, portfolio management and advisory services to the customers; thereby increasing the reach to its customers.

SCL is managed under the overall guidance of its Board of Directors (BoD) who possess wide experience in the financial services. Mr. Apachh Kumar Yadav, Chairman, is a qualified Chartered Accountant and has around 17 years of experience in the banking sector and is associated with SBL in the capacity of Deputy General Manager. Overall management of SCL is led by Mr. Bijaya Lal Shrestha, Chief Executive Office, with merchant banking experience of 18 years. He is supported by an experienced team of professionals.

Professional fund supervisors with experience in their respective field

As per the regulatory eligibility criteria, SBL has appointed five professionals as fund supervisors. Fund supervisors have wide experience in their respective fields. The fund supervisors' panel consists of ex-secretary for Home Ministry Government of Nepal, ex-deputy governor at Nepal Rastra Bank, ex-managing director of Nepal Doorsanchar Company Limited (Nepal Telecom), ex-senior advocate at Supreme Court of Nepal and professionals involved in Audit firms.

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

Diversified investment portfolio and improving merchant banking performances over the period

The investment portfolio of the company has been continuously growing over the past three years. SCL's investment value increased by 22.41% year on year to Rs. 316.12 Mn at the end of FY21 (Audited, refers to the twelve-month period ended mid-July 2022). This has further increased to Rs. 431.13 Mn by the end of 9MFY22 (Unaudited, refers to the nine-month period ended mid-April 2022). Furthermore, SCL's total income increased by 147.97% to Rs. 165.67 Mn during FY21 aided by significant increment in income from issue management, portfolio management and Depository Participant (DP) service coupled with increase in net gain on financial investment as a result of the bullish trend in capital market during FY21. Consequently, income from merchant banking activity increased significantly by 256.73% during FY21. Overall, SCL reported increase in PAT by 180.71% to Rs. 76.45 Mn during FY21. However, the company's earning profile has moderated during 9MFY22 with total income amounting to Rs. 93.91 Mn, impeded mainly by lower than expected revenue from merchant banking activities. The company has a sizeable issue in pipeline, which is likely to add to the income over the near term. During 9MFY22, SCL reported PAT of Rs. 43.90 Mn.

Regulatory support for development of financial markets and mutual fund industry

Finance Act for FY23 has made mandatory provision for requirement of public offering of securities by the companies with capital of Rs.1 Bn or more, or turnover of Rs. 5 Bn or more, or companies that mobilizes natural resources and has them enlisted in the stock exchange. This is likely to help increase the scope of diversification of investment portfolio to be made by mutual funds rather than having the investment concentrated predominantly in the banking, insurance and hydropower sectors. Also, tax exemption has been granted for mutual fund schemes and as per Securities Board of Nepal (SEBON) guidelines, 5% of primary market shares should be allocated to mutual funds (IPOs are mostly made at par) which benefits Net asset Value (NAV) of the MF schemes.

Key Rating Weakness**Volatile investment income**

SCL's investment income has been volatile over FY19-FY21, despite increasing portfolio. SCL had reported Rs. 85.71 Mn income from investments during FY19, which declined to Rs. 34.31 Mn during FY20. Although SCL's investment income increased to Rs. 65.61 Mn during FY21 aided by net gain on financial investment amounting to 56.46% of total investment income. During 9MFY22, it has again moderated to Rs. 30.68 Mn amid the bearish trend of stock market net gain on financial investment is low. Investment portfolio has, however, continuously increased over the period from Rs.216.86 Mn at the end of FY19 to Rs. 431.13Mn at the end of 9MFY22.

Evolving mutual fund industry

Formal issuance of Mutual Fund Schemes started after the issuance of Mutual Fund Regulations, 2067 by SEBON. Currently, there are 25 close ended mutual funds and 4 open ended mutual funds with total AUM of Rs. 32,104 Mn. Further, 10 mutual fund schemes are in the pipeline to be approved from SEBON with a total Assets Under Management (AUM) of Rs. 11,300 Mn. As on May 06 2022, industry average NAV was Rs. 11.07. In case of Sunrise First Mutual Fund (SFMF), NAV stood at Rs. 19.21 as on Mid- July 2021 which decreased to Rs. 13.75 as on Mid- April 2022 and further decreased to Rs. 13.27 as on May 06 2022. Similarly, NAV of Sunrise Blue Chip Fund (SBCF) stood at Rs. 10.06 as on Mid- July 2022 which decreased to 9.51 as on Mid- April 2022 and further decreased to 9.24 as on May 06 2022. Bearish stock market condition due to the ongoing liquidity crisis in the nation has impacted the NAVs of mutual fund schemes. Diversifying investments and associated risk to ensure good returns, ploughing back of returns and enhancing NAV will be the key rating sensitivities.

Volatile trend of NEPSE index

The SFMF and SBCF managed by SCL are equity-oriented schemes and majority of funds collected are being invested in primary and secondary market of Nepal Stock Exchange Limited (NEPSE). NEPSE index has shown volatile trend over the period. The evolving COVID-19 pandemic's impact on the country's economic growth rate coupled with rise of Credit to Deposit ratios in banking industry has resulted in a stretched liquidity situation in the overall economy. Also, monetary policy for FY22 required cap of 4 crore per banks and 12 crore from all the banks in total for margin lending (loan against shares). Cumulatively, these factors have created adverse effect in the capital market. NEPSE decreased from 1,888.36 as on July 27, 2016 (Previous all-time highest index) to 1,336.67 at the end of July 7, 2020 and again reached to new all-time high of 2,883.38 as on July 15, 2021 but again decreased to 1925.12 as on June 28, 2022. Investment diversification to minimize the risk of volatile trend of NEPSE index will be the key rating sensitivities.

Limited market diversification

The schemes launched so far mostly make equity investments through the primary and secondary markets, predominantly in banks, financial institutions and hydro sector. Given the volatility due to lack of equity market depth, the fund managers may face challenges in liquidating the portfolio closer to its valuation upon gain/loss realization thus affecting NAVs of schemes. Further, limited market for bonds and other fixed income securities has created limitation in scope for investment and risk diversification. However, going forward, increasing participation in the capital market by the non-financial sectors meeting the capital and turnover requirements, as required by the Finance Act FY23, is likely to enhance scope for investment and risk diversification.

About the company

Sunrise Capital Limited (SCL) is subsidiary company of Sunrise Bank Limited (SBL) with 100% holding in share capital of SCL. The parent company SBL acquired NIDC Capital Market Limited during February 2017. NCM Merchant Banking Limited, erstwhile subsidiary of NCML becomes subsidiary of SBL. SCL is providing merchant banker depository services, portfolio management services, advisor services and other financial services. SCL has Rs.200 Million paid up capital which has been held by SBL, 'A' Class Commercial Bank of Nepal.

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Annexure 1

CARE Ratings Nepal Limited – Fund Management Quality Rating Scale and Definitions

Symbols	Rating Definition
CARE-NP AMC Quality 1 (AMC1)	AMCs rated AMC 1 are adjudged to have the highest assurance on management quality of AMC.
CARE-NP AMC Quality 2 (AMC2)	AMCs rated AMC 2 are adjudged to have high assurance on management quality of AMC.
CARE-NP AMC Quality 3 (AMC3)	AMCs rated AMC 3 are adjudged to have adequate assurance on management quality of AMC.
CARE-NP AMC Quality 4 (AMC4)	AMCs rated AMC 4 are adjudged to have inadequate assurance on management quality of AMC.
CARE-NP AMC Quality 5 (AMC5)	AMCs rated AMC 5 are adjudged to have poor assurance on management quality of AMC.

Note:

- i. CARE Ratings Nepal's opinion as expressed by way of AMC quality ratings are not a comment on statutory compliance, financial performance or future performance of schemes managed by the Asset Management Company.
- ii. For the quality rating categories 2, 3 and 4, the sign of + (plus) may be appended to the Rating symbol to indicate its relative better position within the Rating categories concerned.