

Suryodaya Womi Laghubitta Bittiya Sanstha Limited

Ratings

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

CARE Ratings Nepal Limited (CRNL) has assigned rating of 'CARE-NP BB (Is)' to Suryodaya Womi Laghubitta Bittiya Sanstha Limited (SWMF). 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 rating assigned to SWMF is constrained by its weak assets quality indicated by surging Gross Non-Performing Loan (GNPL) ratio during FY23 (Unaudited; FY refers to the twelve-month period ending mid-July), high dependence on Banks and Financial Institutions borrowings (BFIs) borrowings, 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 experienced board members, long track record of operations and diversified geographical coverage and sector wise credit portfolio distribution. The rating also factors in adequate capitalization level, moderate liquidity profile and substantial increase in scale of operations over FY21-FY23 aided by organic growth as well as via mergers and acquisitions.

Going forward, the ability of the company to continue its growth momentum along with substantial improvement in asset quality while maintaining capital adequacy ratio will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Weak assets quality

SWMF has a weak asset quality profile marked by high GNPL of 6.78% of total loans and advances as on mid-July 2023, deteriorating from 3.86% as on mid-July 2022. More than 30-days overdue advances of SWMF were also relatively high at 7.47% of total loans and advances as on mid-July 2023. Increasingly stressed asset profile currently observed in the banking industry has exacerbated amid high inflation and interest rates impacting entire demand-supply dynamics for various sectors, leading to reduced debt repayment capabilities of borrowers, and resulting in higher delinquencies. Muted pace of economic growth in the country could result in further slippages in SWMF's asset quality in coming quarters. The MFI's ability to improve collection leading to better asset quality will remain a key monitorable aspect.

High dependence of resource profile on Banks and Financial Institutions (BFIs) borrowings

SWMF's major source of funding consists of deposits from its members and borrowings from banks and financial institutions. The ratio of borrowings to total resource stood high at ~41% as on mid-July 2023, decreased from ~50% as on mid-July 2022. Cost of funds increased to 12.27% in FY23 from 10.37% in FY22. Higher dependence on BFI borrowings increases the cost of funds for the MFI, putting additional pressure on its profitability.

Competition from other MFIs and Co-operatives

As on Mid-March 2023, there were 63 MFIs in operation with total 5,168 branches all over Nepal. SWMF has 192 branches as on Mid-July 2023. Micro Finance Industry earned Rs. 46,902 Mn interest income, Rs. 18,289 Mn net interest income and Rs. 2,991 Mn Net profit till Mid-April 2023. SWMF has 2.49% (Rs. 1,168 Mn) share on interest income, 2.43% (Rs. 444 Mn) share on net

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

interest income and 1.88% (Rs. 56 Mn) share on net profit for the same period in the industry. SWMF has 2.74% and 2.38% market share in terms of deposit base and loan portfolio respectively of microfinance industry as of Mid-April 2023. Furthermore, large numbers 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, SWMF faces competition to tap in a new customer base and to retain the existing customer.

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 more 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 one-third of total lending. SWMF's percentage of collateral loan is 22.30% of total lending as on mid-July 2023 which increased from 17.42% as on mid-July 2022.

Key Rating Strengths

Experienced board members and long track record of operations

SWMF has six directors in its Board of Directors led by Chairman, Mr. Lekha Nath Khaniya, who has around three decades of experience with Nepal Rastra Bank. The company's management team is led by Chief Executive Officer, Mr. Moscha Prasad Pangeni, having experience of more than two decades in Government service in various positions. He is further supported by experienced team to look after various functions in the company. SWMF has operational track record of over a decade under name 'Womi Laghubitta Bittiya Sanstha Limited' before merger with Suryodaya Laghubitta Bittiya Sanstha Limited in FY22.

Adequate capitalization levels and moderate liquidity profile

SWMF's Tier I and overall Capital Adequacy Ratio (CAR) stood at a decent 11.86% and 12.34%, respectively, at the end of FY23 over the minimum regulatory requirement of 4% and 8%, respectively, for microfinance institutions (MFIs). Adequate cushion in the capitalization levels would put the MFI in a better position to absorb any losses, should they materialize, especially given the uncertainty surrounding credit recovery. The MFI's ability to maintain adequate cushion in the capital adequacy ratios will remain critical for its solvency and growth prospect. SWMF has proposed FPO issuance of Rs. 4.67 Mn, which is expected to further improve the CAR of the company. Company has maintained Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR) of 0.59% and 8.21%, respectively, as on mid-July 2023 which is in line with the minimum regulatory requirements for MFIs.

Geographical diversification of business and sector wise credit portfolio distribution, however concentration towards agriculture sector

SWMF has a diversified geographical presence in Nepal with its 192 branches covering 55 districts of Nepal spanning all 7 provinces as on mid-July 2023. Geographically diversified network base enables SWMF to have varied customer base and diversified portfolio and thereby reduces the risk of volatility of a single economic region.

The credit portfolio of SWMF is reasonably diversified with exposure across agriculture, service industry and service industry although agricultural sector accounted for 64.32% of the MFI's total loans and advances portfolio as on mid-July 2023, increased from 61.80% as on mid-July 2022. Advances towards service sector stood at 28.70% as on mid-July 2023, decreased from 30.17% as on mid-July 2022. Relatively higher exposure towards agriculture sector is common for MFIs in Nepal. The recovery in the agriculture sector depends on various factors such as climatic conditions like monsoons, drought and floods, availability of

prices etc. Any adverse climatic conditions or other unfavorable factors which might have an impact on crop production or sales would adversely affect repayment capacity of the borrowers and put added stress on the MFI's asset quality.

Growing scale of operations

SWMF's credit portfolio grew at Compounded Annual Growth Rate of ~49% during FY21-FY23 to Rs. 10,081 Mn as on mid-July 2023. The growth was in part due to addition of new branches, particularly during FY21 and FY22 and in part due to merger between Womi Laghubitta Bittiya Sanstha Limited and Suryodaya Laghubitta Bittiya Sanstha Limited in FY22. SWMF has 2.74% and 2.38% market share in terms of deposit base and loan portfolio respectively, of the microfinance industry as on mid-April 2023. During FY22, SWMF's total income increased by ~89% y-o-y to Rs. 1,107 Mn and the growth momentum persisted with ~52% y-o-y growth to Rs. 1,683 during FY23. The increase in total income is mainly on account of growing loans portfolio and increased interest rates leading to better yields. Consequently, net interest income increased by ~23% to Rs. 579 Mn during FY23.

About the Company

Suryodaya Womi Laghubitta Bittiya Sanstha Limited (SWMF) is a "D" class National Level microfinance institution. It is formed with merger of Womi Laghubitta Bittiya Sanstha Limited and Suryodaya Laghubitta Bittiya Sanstha Limited on April 02, 2022. Womi Laghubitta Bittiya Sanstha Limited was incorporated on June 09, 2011 and commenced its operations on March 08, 2012. SWMF is primarily engaged in providing microfinance loan based on the Joint Liability Group (JLG) model with each group consisting of minimum two members and maximum fifty members.

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