

ROYAL MONETARY AUTHORITY OF BHUTAN

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BHUTANESE FINANCIAL SECTOR PERFORMANCE REVIEW (March 2013 – 2014)

Financial Regulation & Supervision Department

This report presents in general the performance of the Bhutanese financial sector on peer group basis (excluding NPPF) for the period ended Q1FY'14 in comparison to the corresponding quarter of the previous year. This report has been prepared by the Financial Regulation & Supervision Department of the Royal Monetary Authority of Bhutan (RMA) and the information contained in this report is based on the returns submitted by the financial institutions to the RMA. The observations are highlighted below:

1. Overview

Financial institutions remained healthy; credit off-take has picked up, and continued to manage growth with sufficient reserves of capital and liquidity. A number of regulatory measures were announced with a view to tightening the prudential infrastructure, plugging gaps in regulation and ensuring that regulatory and supervisory set up reflected international best practices. With high growth potential, banks have immense opportunities to further expand their business both with traditional and innovative products and through financial inclusion using technology enabled sustainable business models. Finally, sustained pursuit of forward looking strategies aimed at mitigating risks, containing asset-liability mismatches, providing effective response to changing market environment and improving customer relationships should strengthen the overall growth of the financial sector in the medium term.

2. Business size and growth (Financial Sector)

As of March 2014, the total assets of the financial system have expanded to Nu. 89.99 billion as compared to Nu. 82.06 billion in March 2013 indicating a growth of 9.66 percent. The growth has been recorded in the assets of banks which have increased from Nu. 73.24 billion to Nu.79.52 billion, and that of non-banks from Nu. 8.22 billion to Nu. 10.47 billion. However, in terms of the percentage growth of the total assets of banks and non-banks, the bank's total assets increased by 8.58 percent and non-banks increased by 18.65 percent. The composition of the balance sheet of the banks continued to be dominated by traditional balance sheet items. The deposits constituted about 77% of liabilities and loans and advances (net of provision) comprised about 60% of banking assets. The cash and bank balances constitute about 33% of total assets. The investments (securities and equity) which accounted for 4% of assets mostly consisted of Government and RMA securities. For non-banks (insurance companies), 69% of total assets comprises of loans and advances.

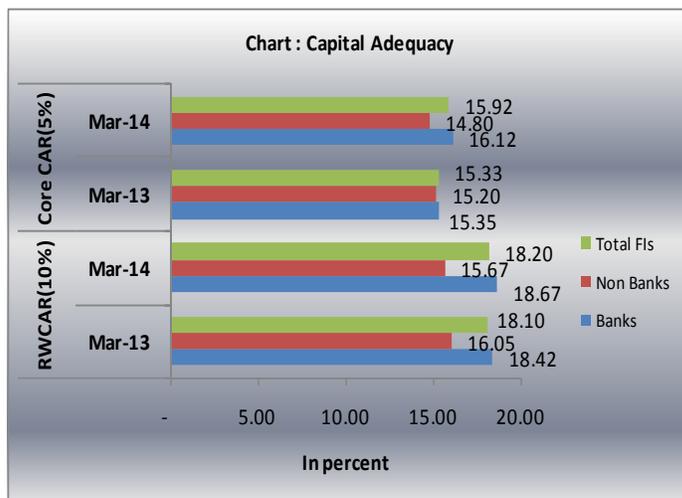
The increase in the total assets of the banks **during the period under review** was mainly contributed by cash and bank balances which has increased from Nu. 20.73 billion in March 2013 to Nu.26.45 billion in March 2014. The loans and advances also increased from Nu. 45.32 billion to Nu.47.92 billion. However, the total investment in Government securities and RMA bills decreased from Nu. 5.52 billion to Nu. 3.06 billion during the period under review. For non-banks the cash and bank balances increased from Nu. 1.53 billion to Nu.1.96 billion (by 27.65 percent) and loans and advances has increased from Nu. 6.08 billion to Nu.7.19 billion (18.07 percent) during the period under review. In terms of the asset composition of financial sector, the banking system constitutes 88.37 percent of the total assets and the remaining 11.63 percent constitutes non-bank's assets.

ASSETS	Banks		Non Banks		Total	
	Mar-13	Mar-14	Mar-13	Mar-14	Mar-13	Mar-14
Cash & Bank Balances	20,731.23	26,445.42	1,528.68	1,951.35	22,259.91	28,396.77
RGOB/RMA Securities	5,524.01	3,056.40	0.00	0.00	5,524.01	3,056.40
Loans & Advances (net of prov)	45,318.08	47,921.90	6,087.48	7,187.64	51,405.56	55,109.54
Equity Investments	242.14	236.14	83.98	115.98	326.13	352.13
Fixed Assets	628.58	741.58	163.89	278.74	792.47	1,020.32
Other Assets	793.56	1,117.48	958.93	934.40	1,752.50	2,051.87
Total Assets	73,237.60	79,518.91	8,822.96	10,468.11	82,060.56	89,987.02

Out of total liabilities of the financial sector, it was observed that the paid up capital increased from Nu. 5.01 billion in March 2013 to Nu. 5.52 billion March 2014 (by 10.35 percent in terms of percentage growth). The deposit liabilities of banks increased by 8.37 percent, from Nu. 54.48 billion to Nu.61.06 billion in March 2014. The borrowing has increased from Nu. 4.7 billion to Nu.5.7 billion during the period under review.

LIABILITIES	Banks		Non Banks		Total	
	Mar-13	Mar-14	Mar-13	Mar-14	Mar-13	Mar-14
Paid-up Capital	4,565.85	5,083.77	440.00	440.00	5,005.85	5,523.77
Reserves	7,875.58	8,251.25	1,441.17	1,693.55	9,316.75	9,944.80
Deposit Liabilities	54,482.46	61,057.07	0.00	0.00	54,482.46	61,057.07
Bonds/Borrowings	1,271.80	1,193.51	3,433.29	4,546.99	4,705.09	5,740.50
Funds/Grants	0.00	0.00	0.00	0.00	0.00	0.00
Provisions	1,321.47	1,691.75	5.06	4.89	1,326.52	1,696.65
Current & Other Liabilities	3,720.43	2,241.55	3,503.45	3,782.67	7,223.88	6,024.23
Total Liabilities	73,237.60	79,518.91	8,822.96	10,468.11	82,060.56	89,987.02

3. Capital & Reserves



The financial system remained satisfactory with risk weighted capital adequacy ratio (RWCAR) of 18.20 percent in March 2014 against the RWCAR of 18.10 percent in March 2013. RWCAR were well above the regulatory requirement –both institution wise and a systemic perspective. The total risk weighted assets of the financial sector increased from Nu. 78.15 billion in March 2013 to Nu.84.32 billion in March 2014. As against the

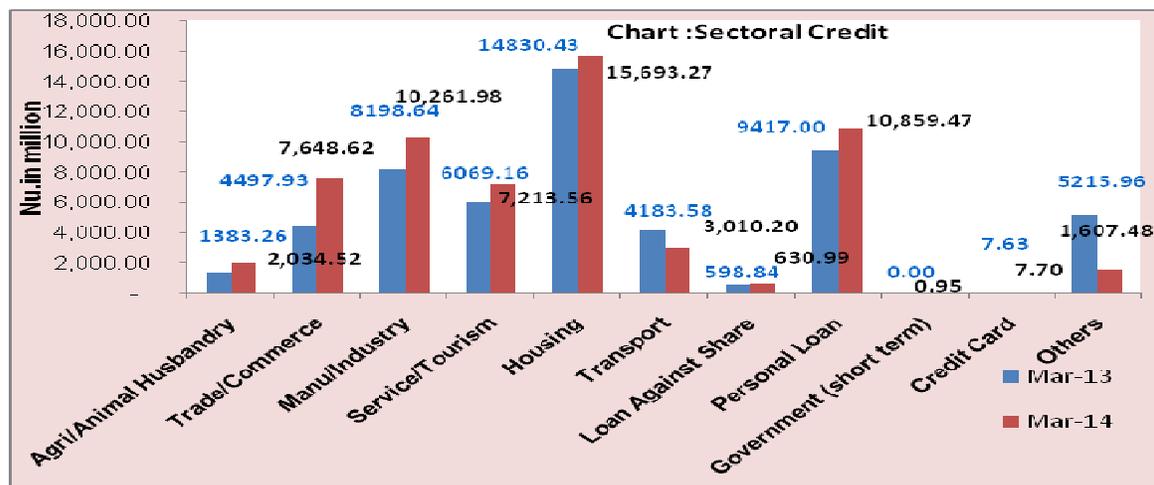
bank's risk weighted assets of Nu. 71.16 billion in March 2014, the paid up capital increased from Nu. 4.56 billion to Nu.5.08 billion with the injection of the equity capital during the period under review. Similarly, the reserves and surplus of the banks slightly increased from Nu. 7.87 billion in March 2013 to Nu.8.25 billion in March 2014. The RWCAR of banks increased slightly from 18.42 percent to 18.67 percent during the period under review.

However, the RWCAR of non-banks has decreased from 16.05 percent to 15.67 percent. The total risk weighted assets of the non-banks has increased from Nu. 10.61 billion to Nu.13.16 billion (24 percent) which has offset the increase in the capital fund of non-banks increased from Nu. 1.70 billion to Nu.2.06 billion (21 percent) during the period under review.

The core capital ratio of the financial sector has slightly increased from 15.33 percent to 15.92 percent during the period under review.

4. Sectoral Credit Analysis (including the credit extension by the non-banks)

The financial system continued to play an active role in providing financing to both the household and corporate/private sectors. During the period ended March, 2014 the financial sectors total lending (gross) to the economy reached to Nu.58.97 billion from 54.4 billion in 2013 or an increase by 8.39 percent. The growth in the lending activity was always attributable to strong demand towards the housing and personal sector, as



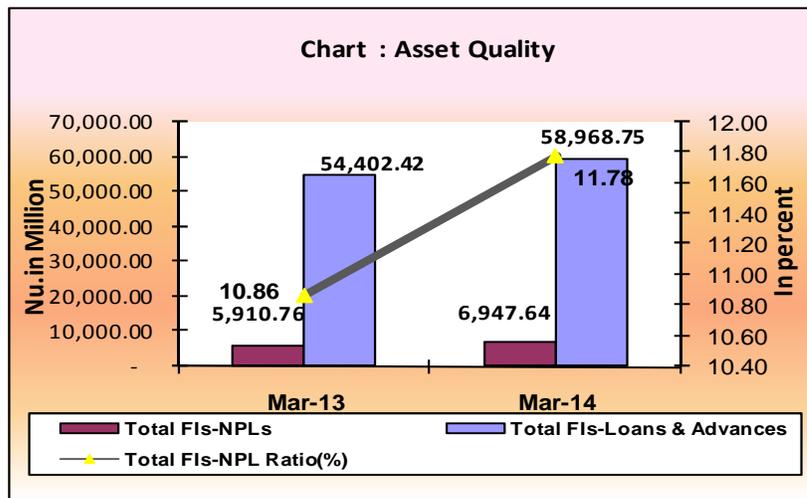
a result leading the other sectoral exposures. The Housing loan increased from Nu. 14.83 billion to Nu.15.69 billion and personal loans increased from Nu. 9.42 billion to 10.86 billion during the period under review.

In terms of the sectoral exposures to total loans and advances, housing sector credit continued to lead the sectoral credit concentration with Nu.15.69 billion (26.61 percent to total loans), followed by personal loan and manufacturing & industry loan with Nu. 10.86 billion (18.42 percent) and Nu. 10.26 billion (17.40 percent) respectively. However, in terms of growth by sector, loans to trade and commerce sector experienced the highest sectoral growth of 70.05 percent (from Nu. 4.49 billion to Nu. 7.65 billion). Agriculture sector is the least credit provided sector by the

financial institutions and constitutes only around 3% of the total loans and advances as of March 2014.

Majority of credit are provided by the banks. Out of total credit of Nu. 58.97 billion, 87.29 percent (Nu. 51.47 billion) are provided by banks and remaining 12.71 percent (Nu. 7.49 billion) are credit provided by non-banks. The total loans and advances provided by the banks has increased from Nu. 48.03 billion to Nu. 51.47 billion indicating a growth of 7.16 percent. Similarly, the total loans and advances of non-banks have also increased by 17.66 percent, from Nu. 6.37 billion to Nu. 7.49 billion during the period under review.

5. Credit Quality (Loans and Advances including the non-banks)

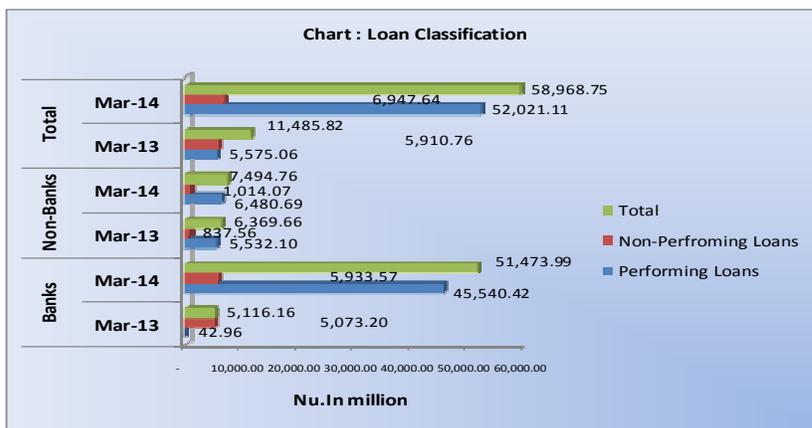


Asset quality continued to pose some concerns as the Non Performing Loans (NPL) of the financial sector grew from Nu. 5.91 billion in March 2013 to Nu. 6.94 billion in March 2014 indicating an increase of 17.54 percent. The NPL to total loans ratio stood at 11.78 percent as compared to 10.86 percent during the period under review. For the period ended

March 2014, the NPL grew by 17.54 percent as against the growth in the total loans and advances by 8.39 percent. Doubtful and loss assets comprised over 54.07 of the stock of NPLs and the remaining 45.93 percent comprised of substandard assets.

Meanwhile, the percentage of provision as a percentage of NPLs provided for impaired loans has increased from 43.90 percent in March 2013 to 48.01 percent in March 2014. The NPL of the banks increased from Nu. 5.07 billion to Nu.5.93 billion as against the increase in the total loans from Nu. 48.03 billion to 51.47 billion during the period under review. The gross NPL ratio of **banks** stood at 11.53 percent as compared to 10.56 percent during the period under review. The NPL for non-banks has also increased from Nu.0.83 billion to Nu.1.01 billion as against the increase in the total loans from Nu. 6.37 billion to Nu. 7.49 billion during the period under review. The NPL ratio of non-banks stood at 13.53 percent as of March 2014.

6. Consolidated Loan Classification of the FIs.

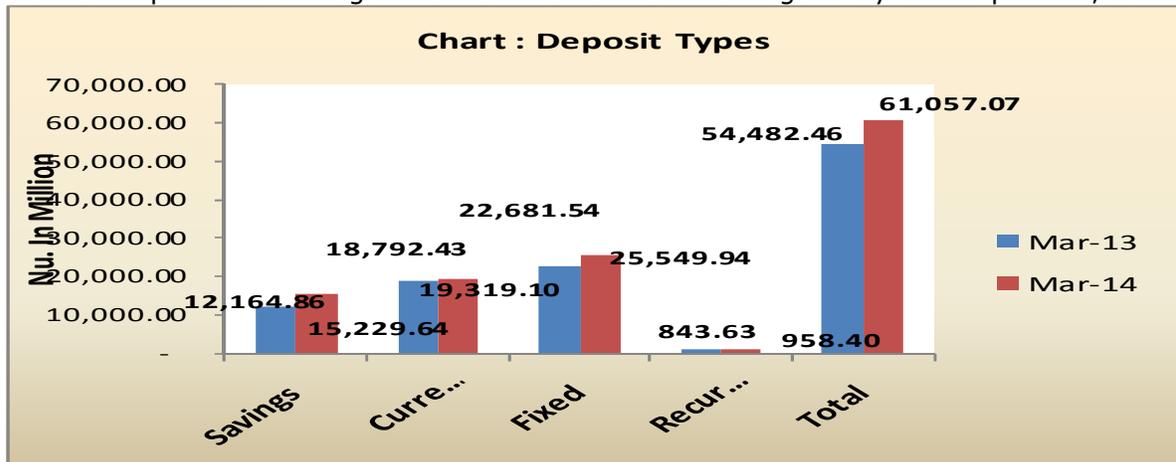


The review on asset classification confirms that around 88.22 percent (Nu.52.02 billion) of total loans (Nu.58.97 billion) disbursed by the financial sector are performing loans and

remaining 11.78 percent (Nu.6.95 billion) are non-performing loans. Of the total loans of Nu. 51.47 billion of banks, 88.47 percent are performing loans and only 11.53 percent are non-performing. Similarly, out of the total loans of Nu.7.49 billion of non banks 86.47 percent are performing loans and the remaining 13.53 percent were non-performing loans for the period under review.

7. Deposits

The total deposit base of the banking sector increased by 12.07 percent, from Nu. 54.48 billion to Nu.61.06 billion during the period under review. The demand deposits which comprises of saving account and current account grew by 11.60 percent, from

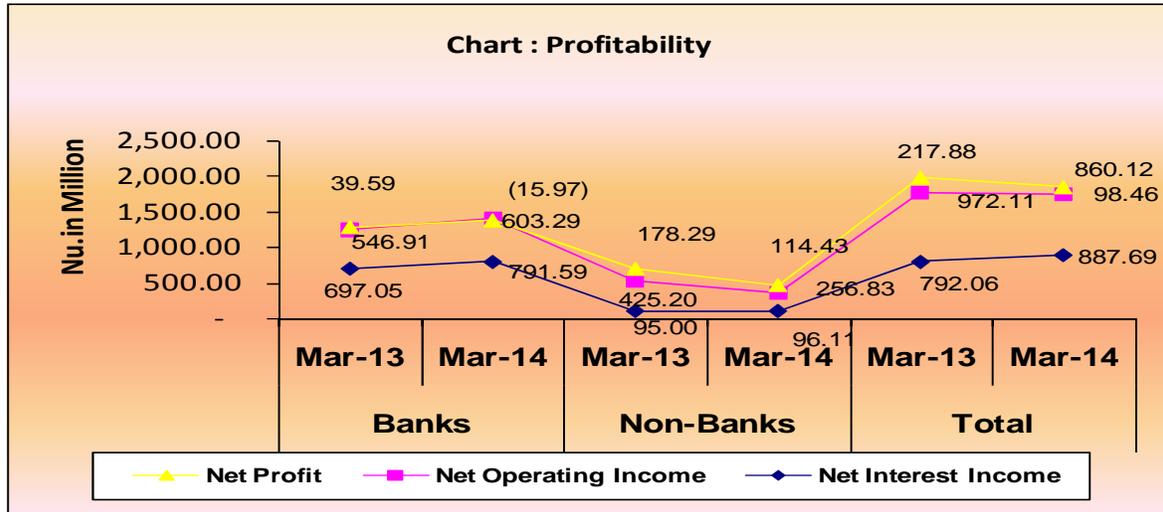


Nu. 30.96 billion in March 2013 to Nu.34.55 billion in March 2014. The time deposits which comprises of fixed and recurring account grew by 12.68 percent, from Nu. 23.53 billion to Nu. 26.51 billion during the period under review.

In terms of customer holdings, corporate deposits accounts for 50.68 percent (Nu. 30.95 billion) of the total deposits and remaining 49.32 percent (Nu 30.11 billion) constitutes retail deposits. In other words, corporate deposits continued to dominate the deposit holding pattern of the financial institutions. As a share of total deposits, demand deposits (current and saving) accounted for 56.56percent and time deposits (fixed and recurring) comprised of 43.42 percent.

8. Profitability

During the 1st quarter 2014, the net profit of the financial sector has decreased when compared to the corresponding quarter of the previous year. The net profit stood at



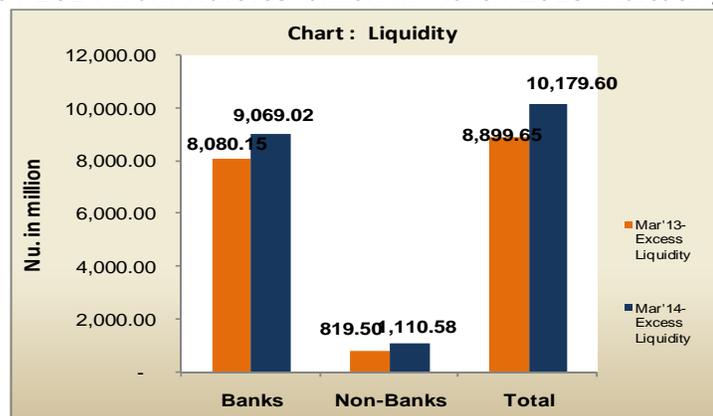
Nu.98.46 million in March 2014 as compared to a Nu. 217.88 million in March 2013. For the first quarter 2014, the banks has incurred a loss of 15.97 million, this is mainly due to huge loss incurred by one of the banks during the period under review. The profit after tax for non-banks stood Nu.114.43 million in March 2014.

The net interest income of the financial sectors has increased from Nu.792.06 million in Q1FY'13 to Nu. 887.69 million in Q1FY'14. However, the net operating income of the financial sector has decreased from Nu.972.11 million in March 2013 to Nu.860.12 million in March 2014, which has led to the decrease in net profit after tax of the financial sector from Nu.217.88 million to Nu.98.46 million during the period under review.

9. Liquidity

On the liquidity front, the excess liquidity of the financial sector has substantially increased to Nu.10.17billion March 2014 from Nu.8.89 billion in March 2013 indicating a growth of 14.38 percent. The increase in liquidity is mainly due to increase in the quick assets from Nu. 21.77 billion in Q1Fy'13 to Nu.24.27 billion (cash & bank balance by 27.57 percent, from Nu.22.26 billion to Nu.28.39 billion) during the period under review.

The statutory liquidity requirement (SLR) of the banks stood at 33.69percent as



compared to 33.29 percent during the period under review and the slight increase in the ratio is mainly due to increase in the quick assets by 10.26 percent from Nu. 20.24 billion to Nu.22.32 billion. Similarly, the statutory liquidity position of non-banks stood at 23.21 percent as compared to 21.56 percent with an slight increase in quick assets from Nu. 1.53 billion to Nu. 1.95 billion during the period under review. The SLR position of both banks and non-banks is above the minimum prudential requirement of 20 percent and 10 percent respectively.