

ROYAL MONETARY AUTHORITY OF BHUTAN

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Financial Regulation & Supervision Department



FINANCIAL SECTOR PERFORMANCE REVIEW REPORT JUNE 2017)

This report presents the performance of the Bhutanese financial sector on peer group basis (excluding NPPF) for the period ended Q2FY'16 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. Further, RMA issued revised Prudential Regulations(PR) 2016 for compliance by all the financial institutions with effect from September 2016. The FRSD has also revised the reporting formats of the financial institutions in line with PR 2016.

Overview

The financial sector continued to grow with an expansion of asset and liability by 19.81%. Total asset of the financial sector has increased by Nu. 24.64 billion, from Nu.124.36billion in June 2016 to Nu. 149.0 billion in June 2017. Out of the total assets of Nu. 149billion, Nu.128.20billion (86.04%) comprised of banks' asset while Nu. 20.80billion (13.96%) comprised of non-banks' asset.

Regarding the performance of financial sector in terms of profitability, it has incurred losses amounting to Nu. 654.13million during the period ended June 2017. The banking sector suffered a loss of Nu.777.89million, while the non-banking sector earned a profit of Nu.123.75million.

The loan provisioning has rapidly increased due to the increase in NPL by Nu.2.92billion. The provision provided for NPLs has almost doubled with Nu. 4.3billion in June 2016 to Nu.6.2billion in June 2017. The loan provisioning requirement for the period ended June 2017 is based on the new loan classification requirement as stipulated under the Prudential Regulations 2016.

Financial sectors' total loans to the economy have increased by Nu.8.45billion during the period under review, which has increased from Nu.86.60billion in June 2016 to Nu.95.06billion in June 2017. In terms of lending by sectors, Housing sector has the highest loan with Nu. 21.70billion (22.83%) followed by Service and Tourism sector with Nu.20.02billion (21.06%) and Trade and Commerce sector with Nu.13.29billion (13.99%). The loan exposures of these three sectors constituted 57.88% of the total loans during June 2017. Similarly, in terms of Non-Performing Loans (NPL) composition, NPL of these three sectors constituted 57.95% of the total NPL. Gross NPL ratio in the financial sector stood at 11.36% in June 2017. Gross NPL ratio of banks and non bank stood at 12.46% and 6.78% respectively.

RMA also issued a new sectoral loan reporting template with effect from 1st November 2016 to capture information on the credit exposure to Micro, Cottage, Small, Medium and Large (MCSML) enterprises. As of June 2017, the share of loan to non-enterprise sector against the total loans was observed to be the highest with 45.91% (Nu.43.64billion), followed by the Medium enterprise with 21.50% (Nu.20.43billion) and large enterprise with 14.81%(Nu.14.02billion). The loan to Micro, Cottage and Small enterprise comprised of 17.78% (16.91billion) of the total loans.

RMA has implemented regulation on microloan institutions and has issued registration certificate to three Microfinance Institutions (MFI) namely Bhutan Association of Women Entrepreneurs (BAOWE), Respect, Educate, Nurture and Empower women (RENEW) and Rural Enterprise Development Corporation Limited (REDCL) as of June 2017. The MFIs have sanctioned a loan to 3151 clients amounting to Nu.227.40million as of June 2017. Out of the total loan outstanding of Nu.165.98million, 515 accounts amounting to Nu.35.31million were under non performing loans.

Capital Adequacy Ratio and Statutory Liquidity Requirement were maintained above the minimum regulatory requirements.

1. Business Size and Growth

1.1. Assets/Liabilities of financial sector

Financial sector continued to grow at the substantial rate with an expansion of asset and liability by 19.81%. Total asset of the financial sector has increased by Nu. 24.64 billion, from Nu.124.36billion in June 2016 to Nu. 149.0 billion in June 2017. Out of the total assets of Nu. 149billion, Nu.128.20billion (86.04%) comprised of banks' asset while Nu. 20.80billion (13.96%) comprised of non-banks' asset. The major component of asset of the financial sector for June 2017 is the net loans and advances (net of provisions) with 58.90% followed by cash and bank balances with 27.85%.

Consolidated statement of condition : June 2016- 2017										
ASSETS	Banks			Non Banks			Total			
	Jun-16	Jun-17	% Change	Jun-16	Jun-17	% Change	Jun-16	Jun-17	% Change	% Holding(June 2017)
Cash & Bank Balances	32,744.72	39,704.47	21.25%	1,906.63	1,797.61	-5.72%	34,651.35	41,502.08	19.77%	27.85%
Marketable Securities	4,138.29	15,226.31	267.94%	60.00	60.00	0.00%	4,198.29	15,286.31	264.11%	10.26%
Loans & Advances (net of prov)	66,662.33	70,132.55	5.21%	14,824.22	17,628.50	18.92%	81,486.55	87,761.05	7.70%	58.90%
Equity Investments	327.30	326.79	-0.16%	253.48	305.23	20.41%	580.78	632.01	8.82%	0.42%
Fixed Assets	1,190.04	1,495.24	25.65%	190.73	220.40	15.56%	1,380.77	1,715.64	24.25%	1.15%
Other Assets	1,139.32	1,318.00	15.68%	924.50	786.51	-14.93%	2,063.83	2,104.51	1.97%	1.41%
Total Assets	106,201.99	128,203.35	20.72%	18,159.56	20,798.25	14.53%	124,361.56	149,001.60	19.81%	100.00%
Liabilities										
Paid-up Capital	7,805.39	7,549.25	-3.28%	1,400.00	1,400.00	0.00%	9,205.39	8,949.25	-2.78%	6.01%
Reserves	10,223.88	9,366.17	-8.39%	1,873.37	2,353.85	25.65%	12,097.25	11,720.02	-3.12%	7.87%
Deposit Liabilities	82,474.39	104,587.56	26.81%	0.00	0.00	0.00%	82,474.39	104,587.56	26.81%	70.19%
Borrowings	703.20	559.05	-20.50%	3,927.52	3,672.59	-6.49%	4,630.71	4,231.64	-8.62%	2.84%
Bonds/Deb	0.00	0.00	0.00%	2,500.00	2,500.00	0.00%	2,500.00	2,500.00	0.00%	1.68%
Provisions	2,563.21	3,202.49	24.94%	16.23	21.56	32.88%	2,579.44	3,224.05	24.99%	2.16%
Funds (*Applicable only for Insurance Companies)					8,264.67			8,264.67		5.55%
Current & Other Liabilities	2,431.93	2,938.83	20.84%	8,442.45	2,585.57	-69.37%	10,874.38	5,524.40	-49.20%	3.71%
Total Liabilities	106,201.99	128,203.35	20.72%	18,159.56	20,798.25	14.53%	124,361.56	149,001.60	19.81%	100.00%

Similarly, on the liability side of the financial sector, the banks' liability consists of Nu.128.20billion of the total liabilities while the non-banks' liability consists of Nu.20.80billion. The major component of the liability of the financial sector was the deposit liabilities of the banking sector with 70.19%.

1.2. Banking sector

Total assets of banking sector stood at Nu.128.20billion in June 2017 as compared to Nu.106.20billion in June 2016 indicating a growth of 20.72% (Nu.22billion). The increase in the asset of the banking sector was mainly due to increase in investment in marketable securities (RMA Tbills) by Nu. 9.96billion. The net loans and advances (net of provisions) of Nu. 70.13billion (54.70%) constituted the major component of assets, while the deposit liabilities of Nu. 104.59billion (81.58%) constituted the major component of liabilities.

1.3. Non-Banking sector

Non-banks also continued to grow with an increase of assets/liabilities by 14.53%. The total assets increased by Nu.2.64 billion, from Nu. 18.16billion in June 2016 to Nu.20.80billion in June 2017. The increase in asset was due to increase in net loans and advances (net of provisions) by Nu.2.80billion. The major component of the asset of the non bank was the loans and advances with 84.76% (Nu.17.63billion).On the liability side, the borrowing from both the commercial banks and non banks by Nu.3.67billion (17.66%) was one of the major main components. As of June 2017, the non-banking sector had an Insurance Fund of Nu.8.26 billion which comprises of the Life Insurance Fund, General Insurance Fund, Group Insurance Fund and other funds.

1.4.Off-balance sheet exposure of financial sector

During the June quarter 2017, off-balance sheet (OBS) exposure of the financial sector accounted for Nu.10.72billion. The share of financial guarantees and other guarantees against total off-balance sheet exposure of the financial sector comprised the highest with 76.38% amounting to Nu. 8.18billion, followed by letter of credit with 23.62% (Nu.2.53billion). For June 2017, the OBS exposure of banking sector accounted for Nu.10.05 billion and the remaining Nu.669.32million accounted for OBS exposure of non-banking sector.

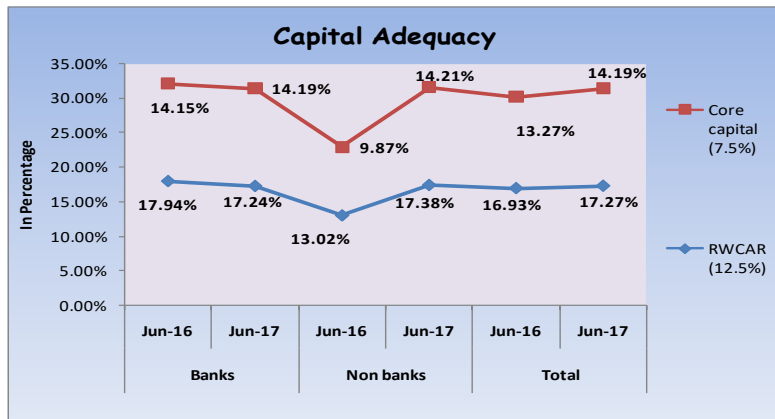
2. Capital and Reserves

Capital serves as a reserve against unexpected losses and is the foundation of sound financial system. Capital base of the financial institution/banks facilitates depositors in forming their risk perception about the institution. Besides absorbing the unanticipated shocks, it also signals that the institution will continue to honor its obligations. Qualifying capital fund is composed of Tier I and Tier II capital. Tier I capital is the financial sector’s core capital, which comprises of paid-up capital and general reserve. Tier II capital is a supplementary capital to Tier 1 capital, which comprises of other reserves, general provisions.

Capital fund¹ of the financial sector for June 2017 amounted to Nu.20.37 billion, as compared to Nu.21billion in June 2016, indicating decrease by Nu.626million. The decrease in the capital fund was mainly due to the withdrawal of government investment in the subordinated term debt as a part of Economic Stimulus Plan (ESP) amounting to Nu.500million from one of the banks. The capital fund of bank amounted to Nu. 16.62billion and for non- banks, it accounted for Nu.3.75billion during the 2nd quarter 2017. In terms of the capital composition, Tier 1 capital, which can absorb the unexpected losses without the financial institution being required to cease operation, consisted of 81.81%(Nu.16.67billion) and remaining 18.19% (Nu.3.71billion) consisted of Tier 2 capital.

2.1 Capital Adequacy

The Risk Weighted Capital Adequacy Ratio(RWCAR) of the financial sector for June 2017 stood at 17.27% as compared to 16.93% in June 2016 showing an increase of 0.34%. The reason for an increase in the CAR was mainly due to the decrease in total risk weighted assets² which was brought about by the reduction of the risk-



¹In this case, the capital fund is the total capital fund without deducting the NPL of related party. The total capital fund and the capital fund for calculating the CAR ratio will not tally since the NPL of related party has been deducted from the capital fund while assessing the RWCAR as required by the section 2.4.7 of PR 2016.

² From September 2016, the Risk weighted asset is computed as per Section 1.8 of the Prudential Regulation 2016 i.e., a risk weight of 100% for performing loans and 150% for non-performing loans

weighted requirements for loans and advances.

Core capital ratio³ of the financial sector, which measures the minimum value of personal risk undertaken by shareholders, has also increased from 13.27% in June 2016 to 14.19% in June 2017. Both the RWCAR and core capital are maintained within the minimum regulatory requirement of 12.5% and 7.5% respectively (With effect from September 2016, minimum requirement on core capital ratio was also increased from 5% to 7.5% including a capital conservation buffer requirement of 2.5%).

2.2 Banking sector

Total Risk Weighted Capital Adequacy Ratio (RWCAR)⁴ of the banking sector has slightly decreased from 17.94% in June 2016 to 17.24% in June 2017. This decrease was mainly due to the decrease in capital fund by Nu.947million which was brought about by loss incurred by banks during the period under review.

Year on Year Growth of Capital adequacy(figure in million Nu)				
	Banks		Non banks	
	Jun-16	Jun-17	Jun-16	Jun-17
Capital Fund	17,488.33	16,541.28	3,273.37	3,740.45
Total Risk Weighted Asset	97,472.76	95,941.54	25,136.46	21,524.11
Tier 1	13,795.16	13,613.49	2,480.63	3,057.64
RWCAR(12.5%)	17.94%	17.24%	13.02%	17.38%
Core capital (7.5%)	14.15%	14.19%	9.87%	14.21%

The RWCAR of the banking sector stood at 17.24% which is 4.74% above the minimum regulatory requirement of 12.5%. The Core capital ratio of the banking sector has slightly increased from 14.15% in June 2016 to 14.19% in June 2017. The ratio was observed to be maintained well above the minimum regulatory requirement of 7.5%.

2.3 Non-Banking sector

RWCAR of non-banking sector has increased from 13.02% in June 2016 to 17.38% in June 2017. The decrease in risk weighted asset by Nu. 3.61billion has led to increase in RWCAR by 4.36%.The core capital ratio of non banking sector stood at 14.21% which was maintained well above the regulatory requirement of 7.5%.

³ With effect from September 2016, financial institutions are required to maintain a minimum core capital of 7.5%., including a capital conservation buffer of 2.5% from Tier 1 capital.

⁴ The RWCAR signifies the availability of capital to support the business of the financial institutions. The NPL of related parties has been deducted from the capital fund when assessing RWCAR as required by the section 2.4.7 of PR 2016.

2.4 Leverage Ratio

Leverage ratio⁵ acts as a supplementary measure to capital adequacy ratio by ensuring that the financial institutions maintain adequate levels of capital at all times. The Leverage ratio for the financial sector for June 2017 stood at 10.44%, maintaining 5.44% higher than the regulatory requirement of 5%. The leverage ratio of banking and non banking sector stood at 10.02% and 14.24% respectively during June 2017.

3. Asset Quality

Quality of asset is one of the most important factor and determinants of the performance and profitability of the financial sector. Since deterioration in the quality of assets has negative impact on the profit, liquidity and capital of the financial sector, assessing asset quality is essential to ensure that assets are stated at reasonable values in relation to the associated risk.

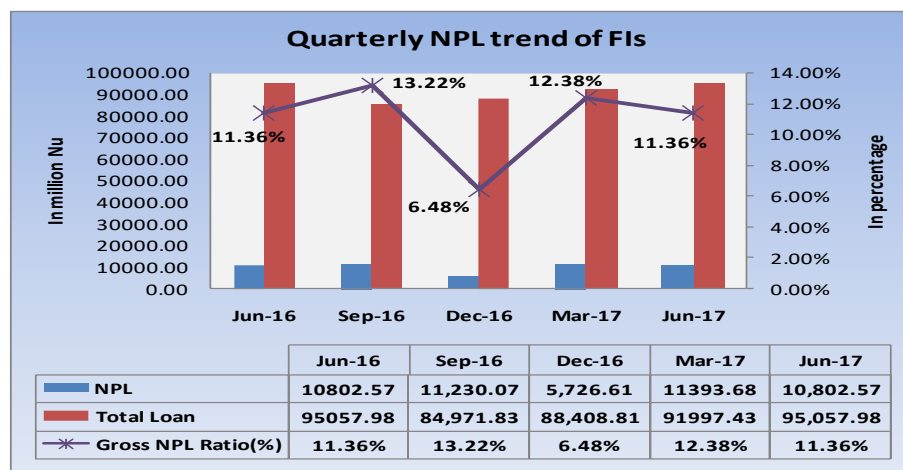
Review on the loan classification of the financial sector indicated that both loans and NPL have increased by Nu. 8.45billion and Nu. 2.92billion respectively during the period ended June 2017. Financial sectors' total loans⁶ to the economy have increased by 9.76%, from Nu.86.60billion in June 2016 to Nu.95.06billion in June2017. The NPL of the financial sector has also increased to Nu.10.80billion in June 2017 as compared to Nu.7.88 billion in June 2016 indicating an increase by 37.12%.

Gross NPL ratio (NPL to total loans) of the financial sector slightly increased to 11.36% in June 2017 as compared to 9.10% in the previous year corresponding quarter. During June 2017, provision coverage ratio stood at 57.82% ,which has increased by 3.11% when compared to June 2016. The increase in the provisions was mainly due to the change in the classification category for loans and advances under the Prudential Regulations 2016, as a result the provision requirements have also been changed.

⁵ From September 2016, the minimum Leverage ratio is raised from 3% to 5%

⁶ With effect from 3rd quarter 2016, Financial institutions are required to submit the monthly returns based on the new PR 2016, i.e., the age days/ bucket has been reduced for doubtful and loss category. The loans and advances whose principal and interest payment has been overdue by 181days to 365days has been included under doubtful category and principal and interest overdue above 365 days has been categorized into loss category.

As shown in the chart below, the NPL depicts an undulating pattern: highest NPL ratio was observed in the month of September 2016 at 13.22% while the lowest was observed



in the month of December 2016 at 6.48%. The NPL ratio for June 2017 has decreased to 11.36% when compared to March 2017 (12.38%). However, when compared to previous year's corresponding quarter (June 2016),

the NPL ratio has increased by 2.26%.

Further, the other component of asset quality, the Single Largest borrower's (SLB) exposure at 15.88% and Ten Largest Borrower (TLB) exposure at 17.39% were maintained within the limit of 30% of capital fund and 30% of the total loans respectively. The net NPL ratio for June 2017 stood at 4.01% as compared to 3.39% in the previous year's corresponding quarter.(Annexure I).

3.1. Asset Quality: banking and non-banking sector

Gross NPL ratio of both banks and non-banks has increased during the period under review. The gross NPL ratio of banks stood at 12.46% in June 2017 as compared to 9.80% in June 2016. Of the total loan outstanding of Nu. 76.72billion in the banking sector, 87.54% (Nu.67.16billion) was regular loans and 12.46% (Nu.9.56billion) was non-

performing loans. The increase in non-performing loans of banks by 34% as against the growth of loan

Consolidated Loan Classification of FIs: June 2016 -June 2017				
Details	Banks		Non Banks	
	Jun-16	Jun-17	Jun-16	Jun-17
Performing Loan	64,435.27	67,161.08	14,290.70	17,094.33
NPL	7,001.07	9,559.29	877.27	1,243.29
Total Loan	71,436.34	76,720.36	15,167.97	18,337.62
NPL Ratio(%)	9.80%	12.46%	5.78%	6.78%

of 7% has led to the increase in gross NPL ratio of the banking sector.

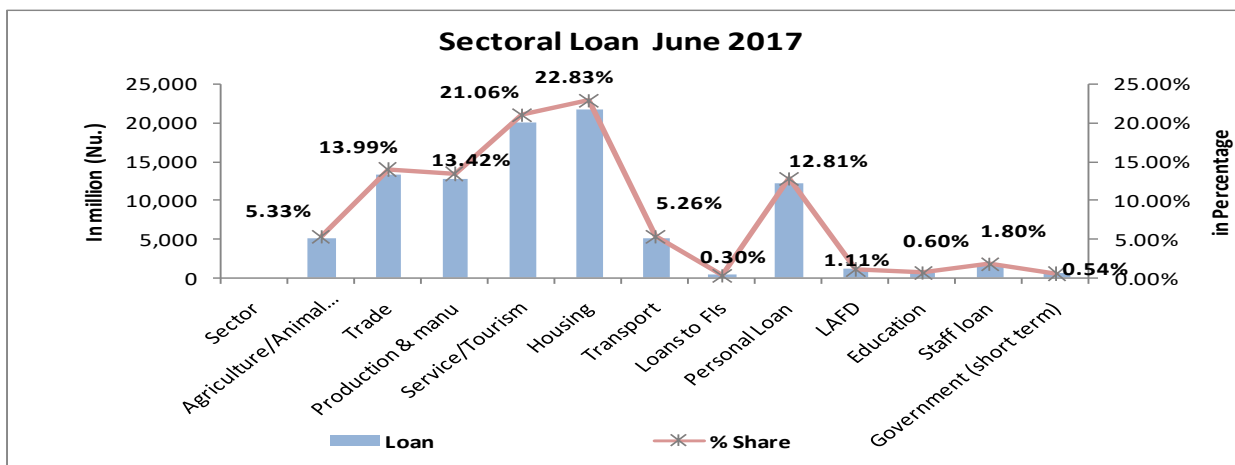
Similarly, the gross NPL ratio of non-banks has also slightly increased to 6.78% in June 2017 as compared to 5.78% in June 2016, an increase by 1%. Of the total loan outstanding of Nu. 18.34 billion of non-banks, 6.78% (Nu.1.24billion) was non-performing loans and remaining 93.22% (Nu. 17.09billion) constitutes regular loans.

4. Consolidated Loan Classification of the Financial Sector

In terms of loan classification by number of overdue days (loan classification category), the highest NPL in the financial sector for the period ended June 2017 was classified under the Loss category⁷ (which also includes the term expired loans and loans under litigation)with Nu.4.88billion (45.17%) followed by Substandard category⁸ with Nu 3.40billion (31.44%) and Doubtful category ⁹ with Nu.2.53billion(23.39%). For banks, the highest NPL was seen under the Loss category with Nu.4.51billion. However, for non banks, the highest NPL was seen in substandard category with Nu.613million.

5. Sectoral Loans and Advances

Loans and advances of the financial sector increased by 9.56% during the period under review. The growth in the loans was attributable towards a strong demand for the Housing sector, Service and Tourism sector and Trade and Commerce sector.



The above diagram shows the analysis on sectoral¹⁰ exposure to total loans and advances of the financial sector, which indicates that out of the total loans of Nu.95.06 billion,

⁷ Loans default from 365 days and above

⁸ Loans default from 91-180 days

⁹ Loans in default from 181 to 365days

¹⁰ For the purpose of this report, Govt. Employee loan (GE),Credit Card are included in the Personal sector and loan against fixed deposits (LAFD) is reflected as a separate sector. LAS have been included under other sectors. Further, Minimum Lending Rate(MLR) was implemented by all FIs in the month of December 2016.

Housing sector has the highest loan with Nu. 21.70billion (22.83%) followed by Service and Tourism sector with Nu.20.02billion (21.06%) and Trade and Commerce sector with Nu.13.29billion (13.99%). The loans under these three sectors jointly constituted 57.88% of the total loans for June 2017.

In terms of increase in loans for the period ended June 2017, the loans to Service and Tourism sector experienced the highest sectoral growth by Nu.8.69 billion followed by Production and Manufacturing sector by Nu.4.07billion and Housing sector by Nu.2.46billion. However, the loans to Trade and Commerce sector and Government short term loan have decreased by Nu.6.08billion and Nu.4.09million respectively.

5.1 Sectoral loan and advances: banking and non-banking sector

From the total loan of Nu. 95.06 billion for the period ended in June 2017, 80.71% (Nu.76.72billion) comprises of loans provided by the banking sector and remaining 19.29% (Nu. 18.34billion) were provided by non-banking sector.

Sectoral Loan of banking and non banking sector: June 2016-June 2017 (figures in Nu. Million)								
Sector	Banks				Non Banks			
	Jun-16	% share June 2016	Jun-17	% share June 2017	Jun-16	% share June 2016	Jun-17	% share June 2017
Agriculture/Animal	4456.90	6.24%	5,061.97	6.60%	0.96	0.01%	7.51	0.04%
Trade	12822.34	17.95%	9,309.34	12.13%	6,548.09	43.17%	3,985.08	21.73%
Production & manu	7086.46	9.92%	10,677.60	13.92%	1,598.15	10.54%	2,079.56	11.34%
Service/Tourism	10560.44	14.78%	15,019.64	19.58%	763.45	5.03%	4,998.30	27.26%
Housing	16217.29	22.70%	18,633.48	24.29%	3,026.74	19.95%	3,071.40	16.75%
Transport	3313.81	4.64%	3,922.36	5.11%	1,221.26	8.05%	1,081.12	5.90%
Loans to FIs		0.00%	281.77	0.37%	0.00	0.00%	0.00	0.00%
Personal Loan	9198.12	12.88%	9,716.98	12.67%	1,429.27	9.42%	2,459.28	13.41%
LAFD	1275.61	1.79%	1,052.88	1.37%	0.00	0.00%	0.00	0.00%
Education	207.94	0.29%	575.07	0.75%	0.00	0.00%	0.00	0.00%
Staff loan	29.09	0.04%	1,222.26	1.59%	0.00	0.00%	493.10	2.69%
Government (short term)	4605.47	6.45%	515.19	0.67%	0.00	0.00%	0.00	0.00%
Others	1662.88	2.33%	731.82	0.95%	580.06	3.82%	162.27	0.88%
Totals	71436.34	100.00%	76,720.36	100.00%	15,167.97	100.00%	18,337.62	100.00%

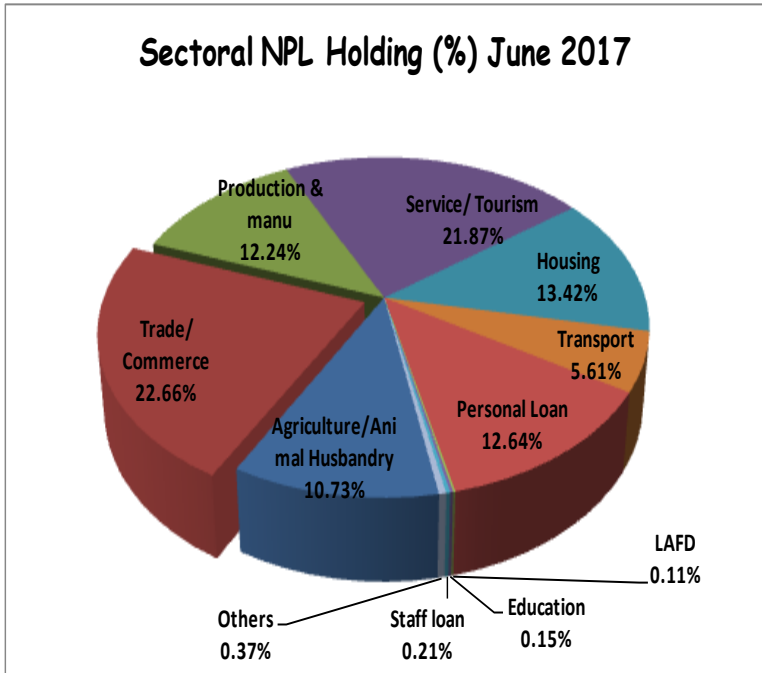
Sectoral loan analysis¹¹ for banking sector for June 2017 reveals that the highest loan was seen in Housing sector amounting to Nu.18.64billion(24.29%) followed by Service and Tourism sector with Nu.15.02billion(19.58%) and Production & Manufacturing sector with Nu.10.68billion (13.92%).

For non-banking sector, the highest loan was seen in Service and Tourism sector with 27.26% (Nu.4.99billion), followed by Trade and Commerce sector and Housing sector with 21.73%(Nu.3.99billion) and 16.75%(Nu.3.07billion) respectively.

¹¹ For June 2016, the return from FIs was based on old reporting format, therefore, the Education loan, Staff loan and loans to FIs were clubbed under other sector. However, for June 2016, the staff loan and education loan could only be segregated for Tbank. For June 2017, the return is based on new reporting format.

6. Credit Quality/ Sectoral NPL of Financial sector

The NPL of the financial sector has increased from Nu.7.88billion in June 2016 to Nu.10.80 billion in June 2017, indicating an increase of 37.12%. The diagram represents the sectorwise NPL holding for the period ended June 2017. The analysis on the sectoral NPL



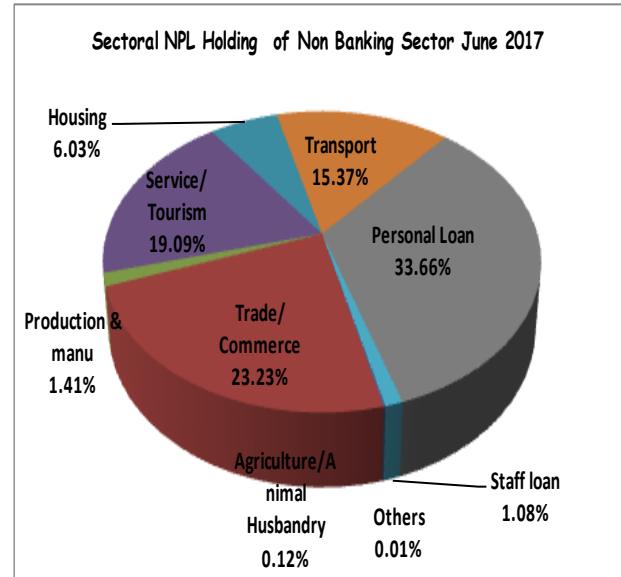
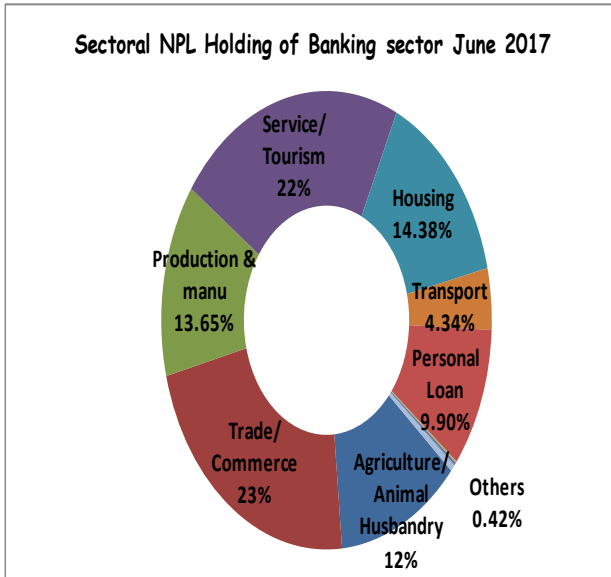
to total NPL of Nu.10.80billion in the financial sector are as follows:

- ✓ Trade and Commerce sector has the highest NPL with Nu.2.45billion (22.66%)
- ✓ Service and Tourism sector with Nu. 2.36billion (21.87%).
- ✓ Housing sector with Nu.1.45 billion (13.42%).

In terms of increase in NPL by sector, Service and Tourism sector represented the highest increase of Nu.978million followed by Agriculture sector with Nu.448 million.

6.1 Sectoral NPL of banking and non-banking Sector

NPL of banking sector has increased from Nu.7billion in June 2016 to Nu.9.56billion in June 2017 indicating an increase of Nu.2.56billion (36.54%). The analysis on the sectoral NPL of banking sector in June 2017 reveals that the highest NPL was seen in Trade and Commerce sector with 23% followed by Service and Tourism sector and Housing sector with 22% and 14% respectively. Similar trend was also noticed in the June 2016, the highest NPL was seen in Trade & Commerce sector with 23% followed by Service and Tourism sector with 19%.

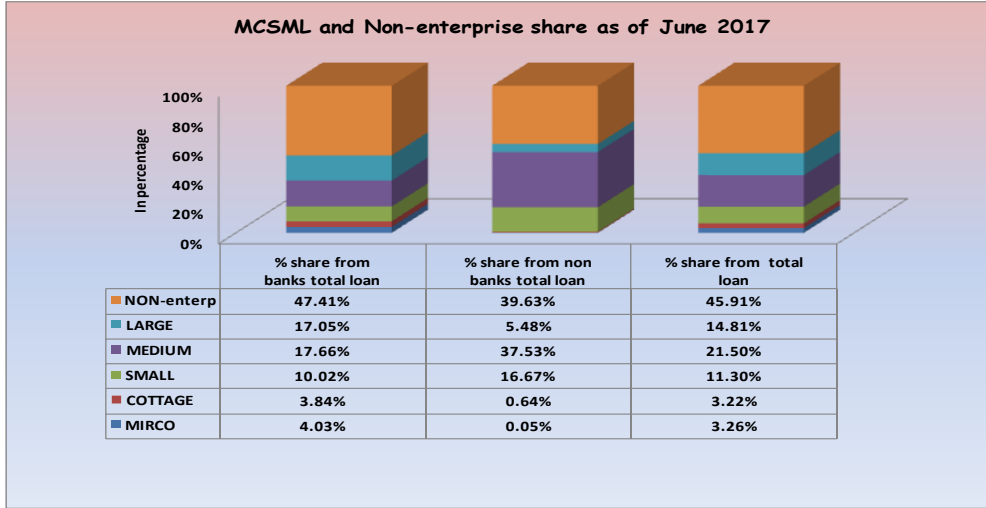


Similarly, the NPL for the non-banking sector increased by Nu.366million, from Nu.877million in June 2016 to Nu.1.24billion in June 2017. Out of total NPL of Nu.1.24billion, the highest NPL during the period under review was seen in Personal Loan¹² with 33.66% (Nu.418million) followed by Trade & Commerce sector with 23.23% (Nu.288million) and Service & Tourism sector with 19.09% (Nu.237million).

¹² For this report, the Sectoral loan and NPL is based on the new reporting format, The personal includes the personal loan ,GE loan and credit card loan..Prior to the new reporting Format, The credit card loan was reflected as different sector, the adjustment are made for both June 2016 and 2017. Further, LAS has been added under other sectors instead of reflecting it as a different sector.These adjustments are made for June 2016 as well

7. Loans to Micro, Cottage, Small, Medium, Large(MCSML) and Non-enterprise loan

With effect from November 2016, all financial institutions were required to submit the information to the RMA based on the new reporting format, of which one of information



required is the loans to Micro, Cottage, small, Medium and Large enterprise (MCSML)¹³ as well as loans to non-enterprise sector¹⁴. As depicted in the diagram below, from the total

loan of Nu.95.06billion, the share of loan to non-enterprise sector against the total loans was observed to be the highest with 45.91% (Nu.43.64billion), followed by the Medium enterprise with 21.50% (Nu.20.43billion) and large enterprise with 14.81%(Nu.14.02billion). The loan to Micro, Cottage and Small enterprise comprised of 17.78% (16.91billion) of the total loans.

Out of the total loan of Nu. 76.72billion of the banking sector for June 2017, the Non-enterprise loan comprised the highest with 47.41% amounting to Nu.36.37billion followed by Medium enterprise with 17.66% (Nu.13.55billion) and Large enterprise with 17.05% (Nu.13.08billion). Loans to Micro, Cottage and Small enterprises consisted only 17.89% amounting to Nu.13.72billion.

Similarly, for non-banking sector, loan to non-enterprise comprised of 39.63%(Nu.7.27billion), the medium and large enterprises constituted of 37.53% (Nu. 6.88billion) and 5.48% (Nu. 1billion) respectively, while loan to small enterprises constituted 16.67% (Nu. 3.06billion). The loan to micro and cottage enterprise consisted only 0.69% (Nu.127million).

¹³ MCSML comprise of Agriculture. Production & Manufacturing, Trade & commerce, Service and Loans to FIs sector.

¹⁴ Non Enterprise sector comprise of Housing, Personal, Transport, staff loan, Education loan, Loan against fixed deposits, Loans to Government and others.

As shown in table below, the highest average growth was observed to be in non enterprise loan with average growth of Nu.42.17billion followed by Medium enterprise with Nu.19.91billion while the lowest growth was observed in cottage enterprise with Nu.2.96billion.

Quarterly Trend of MCSML & non enterprise Loan(figures in Million Nu)				
Loans	Dec-16	Mar-17	Jun-17	Average Growth
MIRCO	2,966.97	2,931.36	3,098.99	2,998.72
COTTAGE	2,688.95	3,137.59	3,062.91	2,960.63
SMALL	9,722.34	10,552.89	10,743.25	10,338.40
MEDIUM	19,245.77	20,055.88	20,433.09	19,911.32
LARGE	13,217.31	13,021.67	14,082.54	13,437.21
NON-enterp	40,567.30	42,298.04	43,637.22	42,167.42
Total	88,408.64	91,997.43	95,057.98	91,821.27

The analysis on the loan trend of MCSML and non enterprise revealed that the Loans to Small, Medium and Non Enterprise saw an increasing trend for all three quarters. However, the loans to Micro and Large enterprise have decreased in March 2017 by Nu.35.61million and Nu.195million respectively when compared to December 2016; these loans perked up in June 2017. On the other hand, the loan to Cottage enterprise which increased till March 2017 showed a decline in June 2017(↓Nu.75million), mainly due to decrease in the agriculture loan which is one of the subsectors of Cottage enterprise.

8. Micro Finance (MFI)

With the implementation of regulation for Microloan institution, RMA has issued registration certificate to three Micro Finance Institutions (MFI) namely; Respect, Educate, Nurture and Empower women (RENEW), Rural Enterprise Development Corporation Limited (REDCL) and Bhutan Association of Women Entrepreneurs (BAOWE). RENEW and REDCL was registered in 2016 and BAOWE was registered as MFI in 2017.

Loans Sanctioned by MFIs as of June 2017(figures in million)			
	No. of Borrowers	Amount Sanctioned	Amount Outstanding
Short term loan (less than 1 year)	1391	62.34	47.90
Long term loan (more than 1 year)	1760	165.06	118.08
Total	3151	227.40	165.98

As of June 2017, the MFIs¹⁵ have sanctioned a loan to 3151 clients amounting to Nu.227.40million. Out of the total loan outstanding of Nu.165.98million, 1760

accounts amounting to Nu.165.06 million was sanctioned as long term loan(more than 1 year) and the remaining 1391 accounts amounting to Nu.62.34million was sanctioned as

¹⁵ The data of MFI is excluding BAOWE

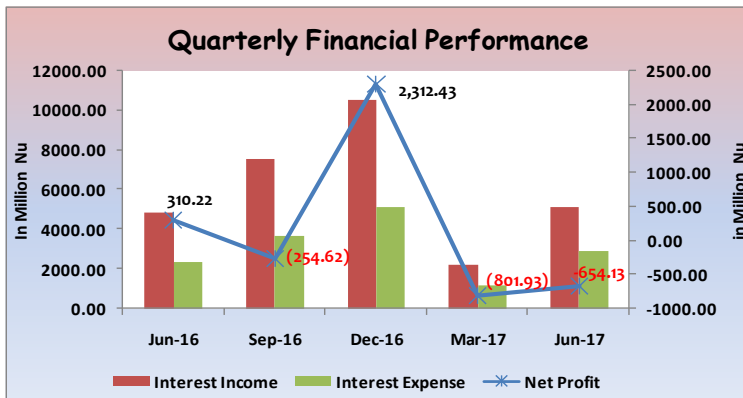
short term loan (less than 1 year). For June 2017, 515 accounts (Nu.35.31million) was under non-performing loan. The gross NPL ratio of MFIs stood at 21.27% (loan of Nu.165.98million, NPL of Nu.35.31million) for June 2017.

9. Financial Performance

One of the important parameters to assess the performance of the financial sector is the earning trend. The continued viability of the financial institutions depends on its ability to earn an appropriate return on its assets, which enables the institutions to fund business expansion and remain competitive.

For the period June 2017, both interest income and interest expenses grew by 5.46% and 22.55% respectively. The loan provisioning has rapidly increased due to the increase of NPL by Nu.2.92billion. This increase in NPL has led to increase in loan provisions which subsequently affected the profitability of the financial institutions. Most banks have incurred losses during the period ended June 2017 that has led to overall losses in the financial sector. The financial sector has incurred a loss of Nu. 654.13million during the period ended June 2017. The banking sector suffered a loss of Nu.777.89million, while, the non-banking sector earned a profit of Nu.123.75million.

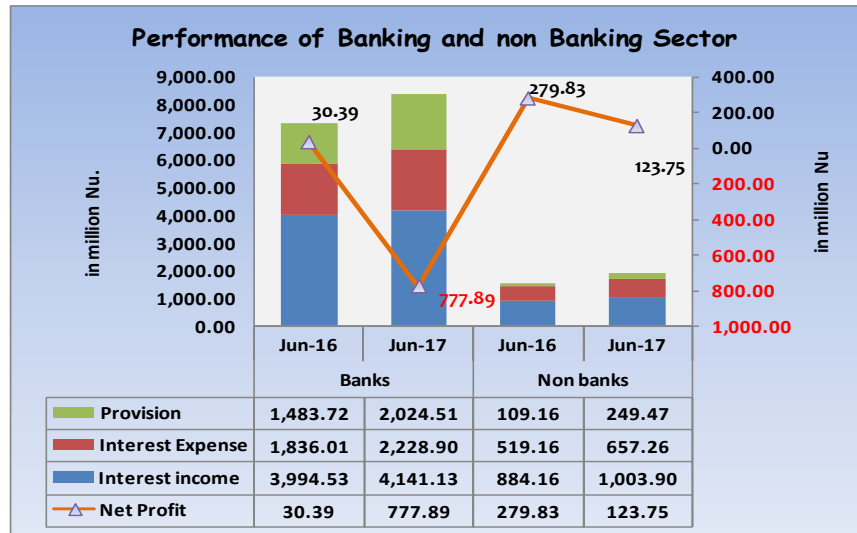
During the quarter, majority of the financial performance indicators, that is, return on assets (RoA) and return on equity (RoE) showed a substantial decline as compared to the previous year corresponding quarter, reflecting the impact of a sharp decline in net profits consequently, reporting a negative RoA of -0.47% and RoE of -3.14%. The RoA and RoE of the banking sector stood at -0.65% and -4.40% respectively. However, the RoA and RoE of the non-banking sector stood at 0.69% and 3.97% respectively.



Looking at the trend of net profit on a quarterly basis, it was observed that net profit of the financial sector depicts an undulating movement. The financial sector usually earns profit towards the year end and incurs losses during the first three quarters.

9.1. Financial Performance: banking and non-banking sector

Banking sector has incurred a loss of Nu.779.89 million in June 2017 as compared to the profit of Nu.30million in June 2016. The substantial increase in NPL by Nu.2.56bllion has resulted to increase in provisioning of Nu.1.62billion which ultimately has contributed towards the deterioration in earnings of the banking sector. Additionally, the increase in interest expense by Nu.392 million has also affected the performance of the banking sector.



Non-banking sector has performed better as compared to the banking sector. The net profit of non-banking sector amounted to Nu. 123million, which has decreased when compared to net profit of Nu.279.83 million in June 2016. Though the NPL of non-banking sector has increased by Nu.366million, it was observed that majority of the NPL was under substandard category that requires a provisioning of only 20%. The interest income for non- banking sector amounted to Nu.1billion while the interest expense amounted to Nu.657million. The interest income from loans and advances amounted to 98% (Nu.986million) and fixed & other deposits accounted to 2% (Nu.17million). The interest expense for bond and borrowings amounted to Nu.171million and the remaining Nu.485million amounted to the expenses incurred for the insurance fund during the period under review.

10. Deposit (Banking Sector)

Deposits are the main source of fund for the banks. The total deposit base of banking sector has increased by 26.81% (Nu.22.11billion), from Nu.82.47billion in June 2016 to Nu.104.59billion in June 2017.

For the period ended June 2017, current and saving account (CASA) deposits has increased marginally as compared to the previous year corresponding quarter. The CASA increased by Nu.1.35billion, from Nu.42.19billion in June 2016 to Nu.55.70billion in June 2017. The Individual and foreign currency accounts constituted the highest CASA accounts with Nu.47.44billion (85% of the total CASA Deposits) and Nu.2.10billion (3.78% of the total CASA deposits) respectively for June 2017.

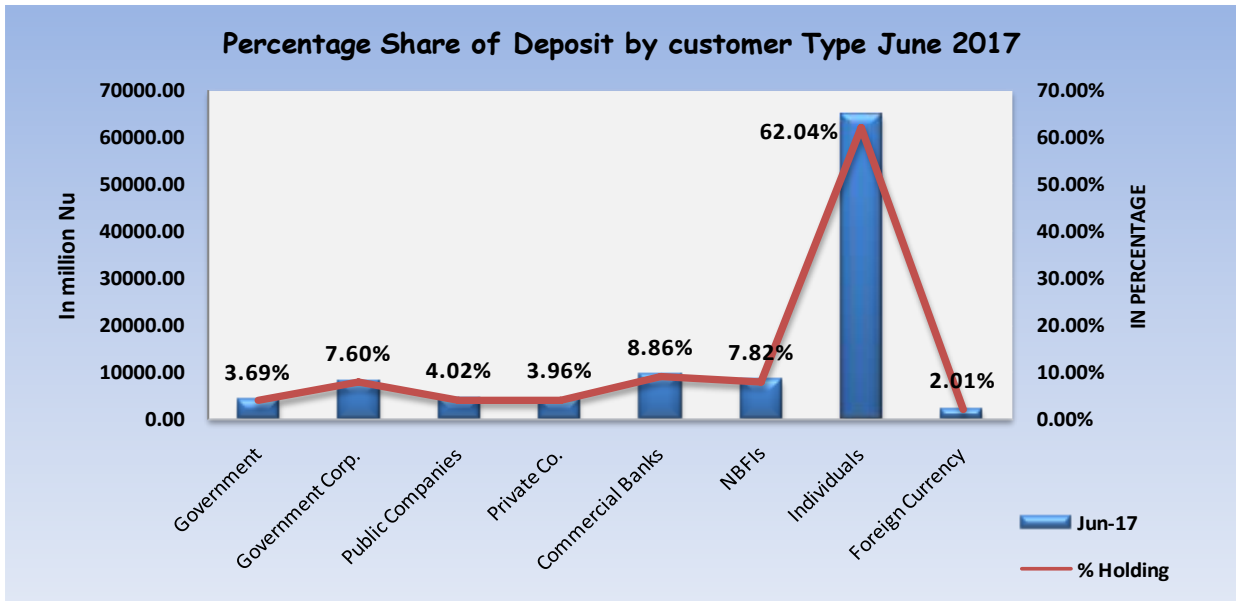
The table below shows the comparison of quarterly deposits trend. The Demand Deposit has increased gradually from Nu 42.19billion in June 2016 to Nu.55.70 billion in June

Deposit by Type (Nu in million)					
	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17
Demand Deposits	42196.84	43841.23	47,395.20	50,409.76	55704.74
Current Deposits	20934.19	21871.22	23,332.05	25,528.03	28721.31
Savings Deposits	21262.65	21970.01	24,063.15	24,881.73	26983.43
Time Deposits	40277.55	42522.86	45,773.38	45,754.76	48882.83
Fixed Deposits	39026.45	41246.21	44,417.16	44,389.02	47449.12
Recurring Deposits	1251.10	1276.64	1,356.22	1,365.73	1433.71
Total	82,474.39	86,364.09	93,168.59	96,164.51	104587.56

2017. Similarly, the Time Deposit also increased from Nu.40.28 billion in June2016, to Nu.48.88 billion in June 2017.

Year-on-year growth(June 2016-june 2017) in the overall deposit base showed that the increase in deposit base was due to the increase in both the Demand Deposits and Time Deposits by 32% and 21% respectively. As a share of total deposits, Demand Deposits (Current and Saving) accounted for 53.26% and Time Deposits (Fixed and Recurring) accounted for 46.74%. Of the total deposit of Nu.104.59billion in June 2017, the Current Deposit accounted for 27.46% while the Saving Deposit accounted for 25.80%. The share of fixed deposit accounted for 45.37% and Recurring Deposit accounted 1.37%.

In terms of deposits by customer, out of the total deposits of Nu.104.59billion in June 2017, Retail Deposits accounted for 64.06% (Nu.66.99billion) and remaining 35.94% (Nu.



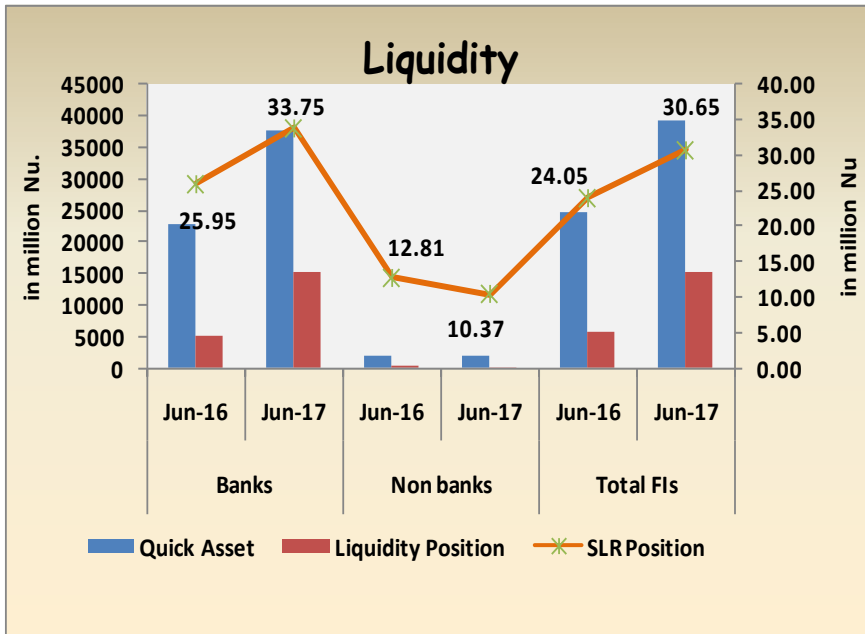
37.59billion) comprises of Corporate Deposits. Out of the total Deposits of Nu.104.59billion, individual deposit constituted the highest with 62.04% followed by the deposits of commercial and non-commercial banks with 8.86% and 7.82% respectively during the period under review. Out of total retail deposits of Nu.66.99billion, individual deposits consists of 96.86%(Nu.64.89billion) and remaining 3.14%(Nu.2.10billion) is in the form of foreign currency deposits. Similarly, out of the total Corporate Deposits of Nu.37.59billion, deposits by Commercial banks constituted the highest with 24.64% amounting to Nu. 9.26billion followed by the deposits of Non-bank financial institutions with 21.76% (Nu.8.81billion) and Government Corporation with 21.13% (Nu.7.94billion) for June 2017.

Credit to Deposit ratio of the banking sector decreased by 13.26%, to 73.36% in June 2017 from 86.62% in June 2016.(Annexure I)

11. Liquidity

It is very important for all financial institutions to have adequate liquidity in order to meet its obligation as and when they fall due. Financial institutions with access to reliable funding sources are likely to expose to low liquidity risk than those having to depend on volatile sources of fund. Further, the Prudential Regulations 2016 requires all banks and non-banks to maintain a minimum statutory liquidity ratio in the form of quick assets of 20% and 10% respectively.

During the period ended June 2017, financial sector has maintained Statutory Liquidity Requirement (SLR) at 30.65%. However as compared to June 2016, SLR of financial sector has increased by 6.6%.



The increase in quick asset by Nu.14.56billion has led to increase in SLR position of the financial sector.

The overall liquidity position of the financial sector remained comfortable by maintaining liquidity in the form of quick assets¹⁶ in excess of the prudent requirement. The quick assets amounted to Nu. 39.43

billion against the minimum requirement of Nu.24.02billion during the period under review.

SLR position of the banking sector stood at 33.75% in June 2017 as compared to 25.95% in June 2016. The increase in the ratio is mainly due to increase in quick asset by Nu.14.70billion which was mostly contributed by increase in the investment in RMA Tills by Nu.9.96billion during the period under review.

The non-banking sector's SLR position as of June 2017 has decreased to 10.37% as compared to 12.81%in June 2016, mainly due to decrease in quick asset by Nu.138million

¹⁶ With effect from 2016, as a transitional stipulation, financial institutions can include time deposits with the remaining period to maturity not exceeding 180 days as a part of quick asset for period of one year

which was specifically attributed by the decrease in demand deposit and time deposit with commercial banks in Bhutan by Nu.199million and Nu.40million respectively. Although the SLR of non-banks has decreased by 2.44%, it is still maintained within the minimum SLR requirement of 10%.

Financial Soundness Indicators of Financial institutions (June 2016-2017)

Indicators	Jun-16	Dec-16	Mar-17	Jun-17
Capital				
RWCAR(12.5%)	16.93%	18.99%	17.84%	17.27%
Core CAR(7.5%)	13.27%	15.58%	15.06%	14.19%
Leverage Ratio	11.80%	11.60%	11.65%	10.44%
Asset Quality				
Gross NPL Ratio	9.10%	6.48%	12.38%	11.36%
Net NPL to Net Loan	3.39%	1.12%	5.46%	4.01%
Single Largest Borrower	14.72%	15.42%	14.61%	15.88%
Ten Largest Borrower	15.85%	16.64%	16.82%	17.39%
Earning				
Return on Asset(ROA)	0.25%	1.82%	-0.61%	-0.47%
Return on Equity(ROE)	1.50%	11.31%	-3.85%	-3.14%
Profit After Tax(in million)	Nu.310.22	2,312.43	Nu.(801.93)	-654.13
Liquidity				
Loans to Deposits ratio	86.62%	77.23%	77.20%	73.36%
Statutory Liquidity Requirement(%)	24.05%	29.30%	31.24%	30.65%
liquidity Position(Nu. In billion)	Nu.5.68	12.52b	Nu.15.54b	Nu.15.41
Statutory Liquidity Requirement(in Nu.billic	Nu.19.18	Nu.21.64	Nu.23.02b	Nu.24.02

Note**** with effect from September 2016, the minimum requirement on RWCAR has been increased to 12.5% from 10% and the minimum requirement on core capital ratio has also increased from 5% to 7.5%

Financial Sector Performance Review Report for June 2017

Annexure II

Year on Year Growth (June 2016-2017) of total financial sector

Particulars	Quarterly Trend (Financial sector)				Figures in Million Nu.	
	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17
Total Capital Fund	20536.00	21003.04	19816.16	21402.73	22055.39	20376.40
Total Assets	130575.05	124361.56	125963.83	137,992.20	145,488.23	149,001.60
Total Risk-Weighted Assets	125061.97	122609.22	110679.55	112391.13	120,154.13	117,465.65
Total Deposits	90992.91	82474.39	86364.09	93168.59	96164.51	104587.56
Total NPLs	8996.62	7878.34	11230.07	5726.43	11393.68	10802.57
Total Performing Loan	70027.85	78725.98	73741.76	82682.21	80603.75	84256.05
Total Loans	79024.47	86604.32	84971.83	88,408.64	91,997.43	95,058.62

Consolidated loan classifications June 2016-2017 (figures in Million Nu.)

	Banks		NBFIs		TOTAL		% Change
	Jun-17	Jun-16	Jun-17	Jun-16	Jun-17	Jun-16	
Performing loans	67161.08	64435.27	17094.33	14290.70	84255.41	78725.98	7.02%
Standard	63666.43	60537.59	10018.70	13043.01	73685.13	73580.60	0.14%
Watch (up to 90 days)	3494.65	3897.69	7075.63	1247.69	10570.28	5145.38	105.43%
Non-performing loans	9559.29	7001.07	1243.29	877.27	10802.57	7878.34	37.12%
Substandard (91 to 180 days)	2783.69	1810.03	613.13	548.03	3396.82	2358.06	44.05%
Doubtful (181 to 365 days)	2264.46	2132.52	262.02	93.84	2526.48	2226.36	13.48%
Loss (366 & above)	4511.14	3058.53	368.13	235.39	4879.27	3293.92	48.13%
Total	76720.36	71436.34	18337.62	15167.97	95057.98	86604.32	9.76%
Gross NPL Ratio	12.46%	9.80%	6.78%	5.78%	11.36%	9.10%	

Financial Sector Performance Review Report for June 2017

Annexure III

Micro, Cottage, Small, Medium, Large (MCSML) and Non enterprise loan for June 2017(in Nu.million)

Sl no.	Sector	Banks			Non Banks			Total FIs		
		Loan Outstanding	% share of each category	% share of total outstanding	Loan Outstanding	% share of each category	% share of total outstanding	Loan Outstanding	% share of each category	% share of total outstanding
(1) MICRO	AGRICULTURE	2,642.21	85.54%	3.44%	0.14	1.43%	0.00%	2,642.36	85.27%	2.78%
	PROD & MANU	47.37	1.53%	0.06%	0.00	0.00%	0.00%	47.37	1.53%	0.05%
	SERVICE	65.83	2.13%	0.09%	2.51	25.03%	0.01%	68.33	2.21%	0.07%
	TRADE&COMMERCE	333.55	10.80%	0.43%	7.37	73.54%	0.04%	340.92	11.00%	0.36%
	LOANS TO FIs	0.00	0.00%	0.00%	0.00	0.00%	0.00%	0.00	0.00%	0.00%
	MICRO TOTAL	3088.96	100.00%	4.03%	10.02	100.00%	0.05%	3098.99	100.00%	3.26%
(2) COTTAGE	AGRICULTURE	1,972.55	66.96%	2.57%	2.11	1.80%	0.01%	1,974.66	64.47%	2.08%
	PROD & MANU	72.90	2.47%	0.10%	2.01	1.71%	0.01%	74.90	2.45%	0.08%
	SERVICE	299.19	10.16%	0.39%	56.06	47.83%	0.31%	355.25	11.60%	0.37%
	TRADE&COMMERCE	601.08	20.41%	0.78%	57.02	48.65%	0.31%	658.10	21.49%	0.69%
	LOANS TO FIs	0.00	0.00%	0.00%	0.00	0.00%	0.00%	0.00	0.00%	0.00%
	COTTAGE TOTAL	2,945.72	100.00%	3.84%	117.19	100.00%	0.64%	3,062.91	100.00%	3.22%
(3) SMALL	AGRICULTURE	380.89	4.96%	0.50%	1.15	0.04%	0.01%	382.04	3.56%	0.40%
	PROD & MANU	1,469.46	19.12%	1.92%	167.69	5.49%	0.91%	1,637.15	15.24%	1.72%
	SERVICE	1,922.31	25.01%	2.51%	1,223.19	40.02%	6.67%	3,145.49	29.28%	3.31%
	TRADE&COMMERCE	3,914.36	50.92%	5.10%	1,664.21	54.45%	9.08%	5,578.57	51.93%	5.87%
	LOANS TO FIs	0.00	0.00%	0.00%	0.00	0.00%	0.00%	0.00	0.00%	0.00%
	SMALL TOTAL	7,687.01	100.00%	10.02%	3,056.23	100.00%	16.67%	10,743.25	100.00%	11.30%
(4) MEDIUM	AGRICULTURE	66.31	0.49%	0.09%	4.12	0.06%	0.02%	70.43	0.34%	0.07%
	PROD & MANU	3,250.35	23.99%	4.24%	1,336.85	19.42%	7.29%	4,587.20	22.45%	4.83%
	SERVICE	6,970.58	51.44%	9.09%	3,379.77	49.11%	18.43%	10,350.35	50.65%	10.89%
	TRADE&COMMERCE	3,263.32	24.08%	4.25%	2,161.80	31.41%	11.79%	5,425.12	26.55%	5.71%
	LOANS TO FIs	0.00	0.00%	0.00%	0.00	0.00%	0.00%	0.00	0.00%	0.00%
	MEDIUM TOTAL	13,550.56	100.00%	17.66%	6,882.53	100.00%	37.53%	20,433.09	100.00%	21.50%
(5) LARGE	AGRICULTURE	0.00	0.00%	0.00%	0.00	0.00%	0.00%	0.00	0.00%	0.00%
	PROD & MANU	5,837.52	44.64%	7.61%	573.02	57.05%	3.12%	6,410.54	45.52%	6.74%
	SERVICE	5,761.74	44.06%	7.51%	336.78	33.53%	1.84%	6,098.52	43.31%	6.42%
	TRADE&COMMERCE	1,197.03	9.15%	1.56%	94.67	9.43%	0.52%	1,291.71	9.17%	1.36%
	LOANS TO FIs	281.77	2.15%	0.37%	0.00	0.00%	0.00%	281.77	2.00%	0.30%
	LARGE TOTAL	13,078.06	100.00%	17.05%	1,004.47	100.00%	5.48%	14,082.54	100.00%	14.81%
Non-Enterprise	HOUSING	18,633.48	51.23%	24.29%	3,071.40	42.26%	16.75%	21,704.88	49.74%	22.83%
	TRANSPORT	3,922.36	10.78%	5.11%	1,081.12	14.88%	5.90%	5,003.48	11.47%	5.26%
	PERSONAL	9,716.98	26.72%	12.67%	2,459.28	33.84%	13.41%	12,176.26	27.90%	12.81%
	STAFF LOAN	1,222.26	3.36%	1.59%	493.10	6.79%	2.69%	1,715.36	3.93%	1.80%
	Education Loan	575.07	1.58%	0.75%	0.00	0.00%	0.00%	575.07	1.32%	0.60%
	Loan Against Fixed Deposits	1,052.88	2.89%	1.37%	0.00	0.00%	0.00%	1,052.88	2.41%	1.11%
	Loans to the Govt	515.19	1.42%	0.67%	0.00	0.00%	0.00%	515.19	1.18%	0.54%
	OTHERS	731.82	2.01%	0.95%	162.27	2.23%	0.88%	894.09	2.05%	0.94%
	Non- Enterprise TOTAL	36,370.05	100.00%	47.41%	7,267.17	100.00%	39.63%	43,637.22	100.00%	45.91%
	GRAND TOTAL	76,720.36			18,337.62			95,057.98		

Sectoral Loan Trend June 2016-June 2017

Sectoral Loan	Jun-16	Dec-16	Mar-17	Jun-17	Holding(June 2017)
Agriculture/Animal Husbandry	4,457.86	4,630.06	4,894.28	5,069.48	5.33%
Production and Manufacturing	8,684.61	11,043.60	12,476.70	12,757.16	13.42%
Service/Tourism	11,323.89	16,677.38	18,242.20	20,017.94	21.06%
Trade/Commerce	19,370.43	15,241.71	13,093.69	13,294.41	13.99%
Loan to FI(s)	0.00	1,394.05	992.52	281.77	0.30%
Housing	19,244.02	20,307.53	20,859.59	21,704.88	22.83%
Transport	4,535.07	4,231.09	4,690.25	5,003.48	5.26%
Personal Loan	10,627.39	10,585.63	12,149.00	12,176.26	12.81%
Staff Loan	29.09	1,610.91	1,656.15	1,715.36	1.80%
Education Loan	207.94	384.90	352.39	575.07	0.60%
LAFD	1,275.61	907.48	1,142.89	1,052.88	1.11%
Loans to Government	4,605.47	513.63	502.65	515.19	0.54%
Others	2,242.94	880.85	945.11	894.09	0.94%
Total	86,604.32	88,408.81	91,997.43	95,057.98	100.00%

***For the purpose of this report, the sectoral loan classification is based on the new reporting format submitted by Fis, where the LAFD is deducted from Personal and shown as a separate sector. LAS is added under other Sectors. Education loan and staff loan is reflected as a new sector instead of clubbing it under other sectors. The same adjustment has been made for June 2016, however, staff and education loan could only be segregated for June 2016 from the old reporting format

Sectoral NPL Trend June 2016-June 2017

Sectoral NPL	Jun-16	Dec 2016	Mar-17	Jun-17	Holding (March 2017)
Agriculture/Animal Husbandry	710.65	542.35	937.51	1,159.08	10.73%
Production and Manufacturing	1,212.37	533.38	1,443.49	1,321.98	12.24%
Service/Tourism	1,384.24	1,156.07	2,428.29	2,362.75	21.87%
Trade/Commerce	2,012.72	1,434.79	3,025.42	2,447.66	22.66%
Loan to FI(s)	0.00	0.00	0.00	0.00	0.00%
Housing	999.39	921.70	1,788.33	1,449.91	13.42%
Transport	506.53	320.59	654.34	605.71	5.61%
Personal Loan	993.80	777.83	1,054.86	1,365.00	12.64%
Staff Loan	0.00	25.42	20.01	22.70	0.21%
Education Loan	0.00	8.32	8.81	16.36	0.15%
LAFD	10.09	3.67	13.57	11.46	0.11%
Loans to Government	0.00	0.00	0.00	0.00	0.00%
Others	48.55	2.31	19.04	39.95	0.37%
Total NPL	7,878.34	5,726.43	11,393.68	10,802.57	100%
Total Loan	86,604.32	88,408.81	91,997.43	95,057.98	
Gross NPL Ratio	9.10%	6.48%	12.38%	11.36%	