

ROYAL MONETARY AUTHORITY OF BHUTAN

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Bhutanese Financial Sector Performance Review (March 2011- 2012)

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Introduction

This report presents in general the performance of the Bhutanese financial sector on peer basis (excluding RSEBL) for the first quarter of 2012 in comparison to the corresponding quarter of the previous year. The information contained in this report is based on the returns submitted by the financial institutions to the RMA. The observations are summarized below:

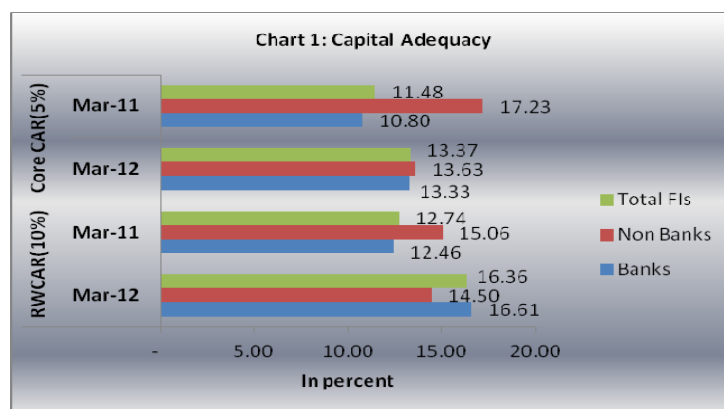
1. Business size and growth.

The total assets of the financial system¹ has expanded by 8.68 percent during the period under review and stood at Nu.84.68 billion as of March 2012 compared to Nu.77.93 billion during corresponding quarter of the previous year.

Assets of both banking system and the non-bank financial institutions (NBFIs) expanded during the first quarter, 2012. Assets of banking system rose by Nu. 3.48 billion, or 5.69 percent, while assets of NBFIs grew by Nu. 3.27 billion, or 19.72 percent. The share of NBFIs in the total financial system assets continued to increase, rising to 23.45 percent in March, 2012 from 21.29 percent in March, 2011. Within the banking system, the increase in the assets was due to the growth in assets of the banks constituting of 76.55 percent to the total financial system assets. This reflected mainly the increase in loans and advances by Nu. 11.15 billion (36.02 percent). Similarly the expansion in the assets of the NBFIs was mainly due to increase in the liquid assets by Nu.373.34 million (48.83 percent) and increase in loans and advances by Nu. 368.80 million (7.34 percent) during the period under review.

Out of the total liabilities of the financial sector amounting to Nu.84.68 billion, majority of it comprises of deposit liabilities with Nu. 50.27 billion (59.37 percent) followed by capital and reserves with Nu. 10.28 billion (12.15 percent). Although the major financial liabilities constitutes of deposits, it was observed that the deposit liabilities in the bank slightly increased by 0.21 percent, from Nu. 50.16 billion in March, 2011 to Nu. 50.27 billion in March, 2012.

2. Capital & Reserves



The financial system remained satisfactory with risk weighted capital adequacy ratio (RWCR) of 16.36 percent in March 2012 against the RWCR of 12.74 percent in March, 2011. Audited profit and accumulated reserves has resulted in the increase in capital base of the financial institutions. The capital fund of financial system

¹ The financial system comprises of BNBL, BOBL, DPNBL, Tbank, BDFCL, RICBL & NPPF

has increased to Nu.10.23 billion in March 2012 from Nu.6.83 billion in March 2011. The increase is seen in banks with 53.47 percent from Nu.5.98 billion to Nu.9.17 billion in March 2012, and the increase was mainly due to the increase in the core capital (paid-up capital by Nu. 0.32 billion and general reserves by Nu. 2.68 billion). Similarly, the non-banks capital fund has increased by Nu.0.24 billion (28.76 percent) during March 2012. However, despite the increase in the capital base of the non-banks, the position of the regulatory capital requirement (RWCAR) has deteriorated to 14.50 percent from 15.06 percent during the period under review. This is due to increase in risky assets (Nu.1.90 billion) vis-à-vis an increase in capital fund (Nu.0.24 billion).

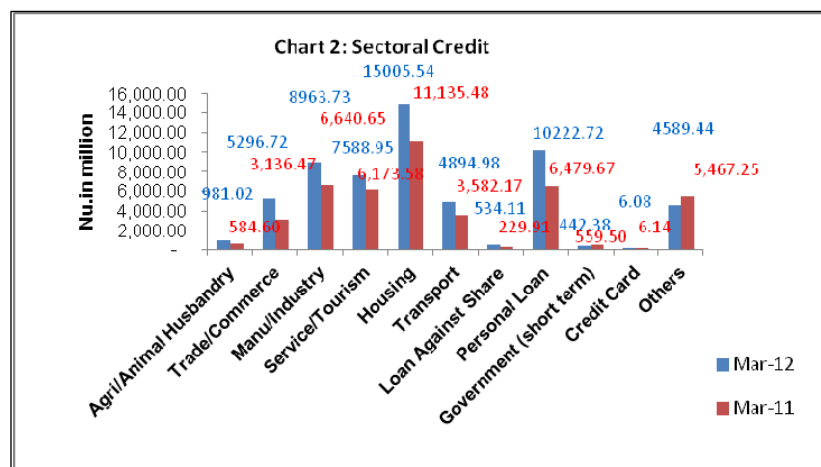
The total risk weighted assets of the financial system increased to Nu. 62.77 billion from Nu. 53.60 billion during the period under review, out of which 87.96 percent comprises of risky assets within the banking sector. Similarly, the core capital ratio has also increased to 13.37 percent to 11.48 percent during the period under review.

3. BANKING

The balance sheet in the Bhutanese banking sector have increased to Nu.64.83 billion from Nu.61.34 billion during the period, indicating a growth of 5.69 percent. The composition of the balance sheet of the banks continued to be dominated by traditional balance sheet items. The deposits constituted nearly 77.55 percent of liabilities and loans and advances (net of provision) comprised about 64.93 percent of assets. The investment (securities and equity) which accounted for 5.01 percent of assets, mostly consisted of Government and RMA securities. The increase in the total resources of the banks was mainly channeled into loans and advances. Total Credit (gross loan and advances) grew at 33.03 percent (including the credit provided by the non-banks) during the period under review from Nu. 43.99 billion to Nu. 58.53 billion during the period under review. The total credit of the bank grew at 36.19 percent, from Nu. 32.67 billion to Nu. 44.49 billion during the period under review. Contrary, the deposits of the banks grew at 0.21 percent.

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

The banking system continued to play an active role in providing financing to both the household and corporate sectors. The total credit (gross) by the financial institutions grew at 33.03 percent, from Nu. 43.99 million in March, 2011 to Nu. 58.53 billion in March, 2012. The lending activity was attributable to the strong

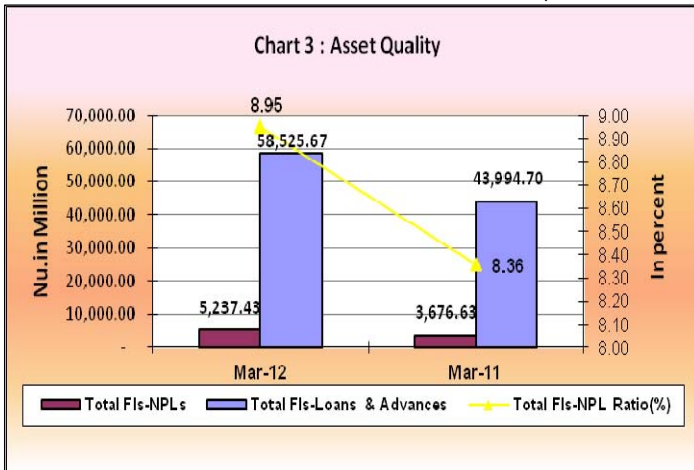


performance in lending to the housing and personal sector, as a result leading the other sectoral exposures. This resulted in strong growth to housing sector by 34.75 percent (from Nu. 11.14 billion in March, 2011 to Nu. 15.01 billion in March, 2012) and personal sector by 57.77 percent (from Nu. 6.48 billion in March, 2011 to Nu. 10.22

billion in March, 2012). This was followed by manufacturing/industry from Nu. 6.64 billion to Nu. 8.9 billion, and service/tourism from Nu. 6.17 billion to Nu. 7.59 billion during the period under review. Almost all the sectors experienced a growth in the loans and advances during the period under review.

b) Asset Quality (Loans and Advances)

Asset quality continued to pose some concerns as the NPL of the financial sector deteriorated by 42.45 percent. Against the total loans of Nu. 58.53 billion, the NPL increased from Nu. 3.68 billion in March, 2011 to Nu. 5.24 billion in March, 2012.

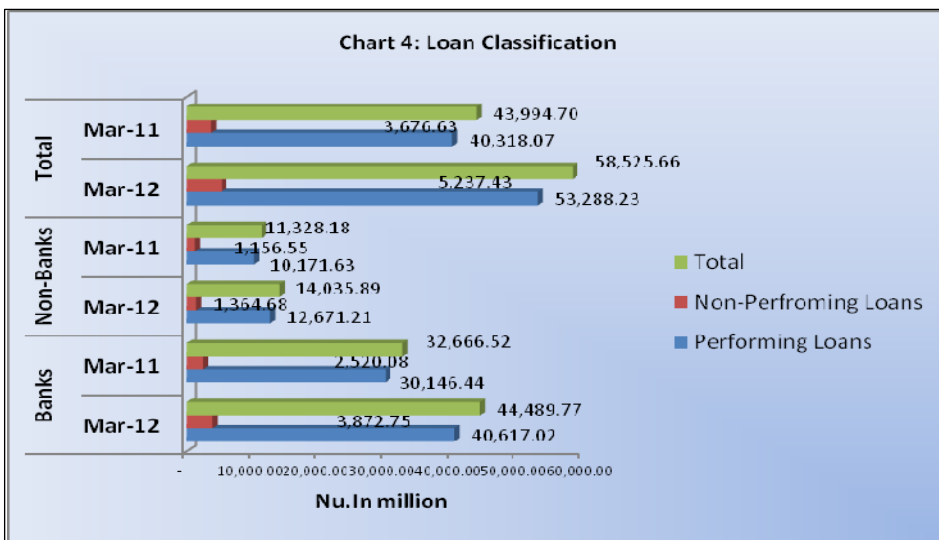


Sub-standard assets comprised over 60 percent of the stock of NPLs and remaining consisting of doubtful and loss assets. The NPL to gross loans and advances ratio increased to 8.95 percent from 8.36 percent during the period under review. The non-performing loans of banks has increased by Nu.1.35 billion (53.68 percent), while that of non-banks by Nu.0.21 billion (18 percent) as well. Similarly, the NPL ratio of the financial system increased from 8.36 percent to

8.95 percent.

Meanwhile, the percentage of provision provided for impaired loans has decreased from 55.80 percent to 48.46 percent in March 2012 (although the specific provision increased from Nu. 2.05 billion to Nu. 2.54 billion during the period under review), mainly due to the classification of NPL into the recent buckets of NPL categorization which requires minimal provision requirement.

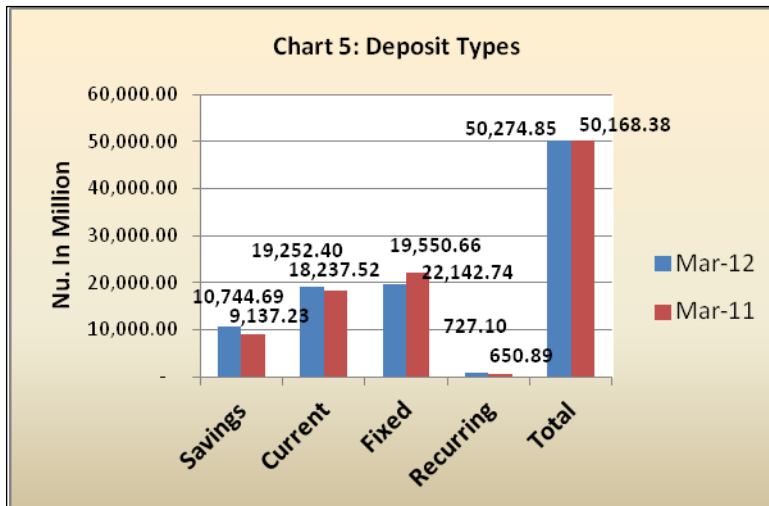
c) Consolidated Loan Classification of the FIs



Analysis on asset classification confirms that around 91.05 percent of total loans disbursed by the financial sector are performing loans. Of the total loans of Nu.44.48 billion of CBs, 91.30 per cent are performing

loans and the remaining 8.70 percent are non-performing. Similarly, 90.28 percent of the total loans and advances (Nu.14.04 billion) of the non banks are performing loans and the remaining 9.72 percent is non-performing loans.

d) Deposits



Total deposit liabilities of the banking sector (including Bhutan Development Bank Ltd.) rose slightly by 0.21 percent (Nu.50.27 billion in March 2012 from Nu.50.16 billion in March 2011). This was mainly due to decrease in the share of time deposits (Fixed and Recurring) by Nu. 2.52 billion (-11.04 percent) during the period under review. However, the share of CASA product (Current and Saving) grew by Nu. 2.62 billion (9.58 percent).

In terms of deposits by customer holding, corporate deposits² accounts for around 57.62 percent and the remaining 42.38 percent constitutes the retail deposits. In other words, corporate deposits have dominated the deposit holding pattern of the financial institutions. As a share of total deposits, demand deposits (current and saving) accounted for 59.67 percent and time deposits (fixed and recurring) comprised of 40.33 percent.

² Corporate Deposits – refers to government, government corporations, joint corporations, private companies, NBFIs and CBs.

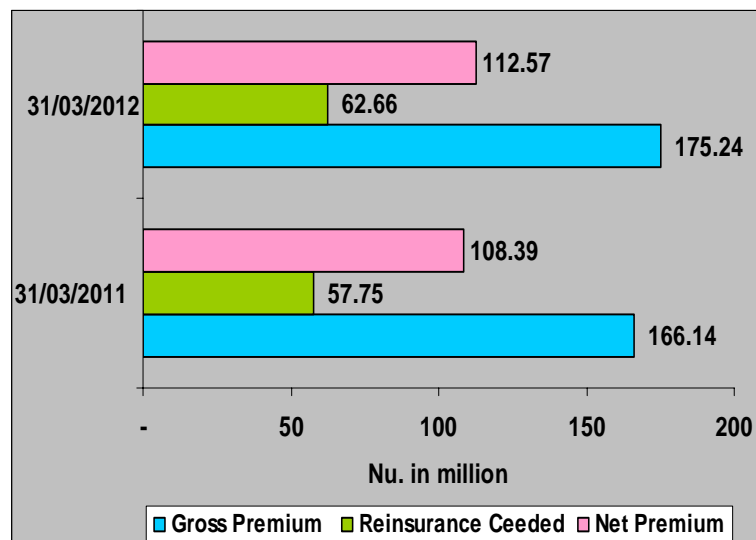
4. INSURANCE

Bhutanese insurance industry, which comprises of Royal Insurance Corporation of Bhutan (established in 1976) and a newly opened general insurance company, Bhutan Insurance limited (established in 2009) is unique in itself because both the insurance companies provides not only insurance services but it also give out retail loans and advances.

1. General Business

Bhutan Insurance companies have seen 100 percent growth in the number of policy holders. The number of policyholders reached 23,711 in March 2012 from 11,821 a year earlier.

Gross premium written increased 5.48 % from Nu.166.14 million in March 2011 to Nu.175.24 million in 2012, mainly due to launching of new products and writing of new business. However, about 35.76 % of total general business has been ceded to reinsurance companies outside the country. On the other hand, claim paid out has considerably increased by about 46 % and stood at Nu.169.52 million in March 2012.



2. Life Business

RICBL achieved strong Gross Written Life Premium growth 47.18% to Nu.61.57 million in March 2012 from Nu.41.84 million in March 2011 primarily through new business acquisition. The number of policyholders stood at 30355 as of March 2012.

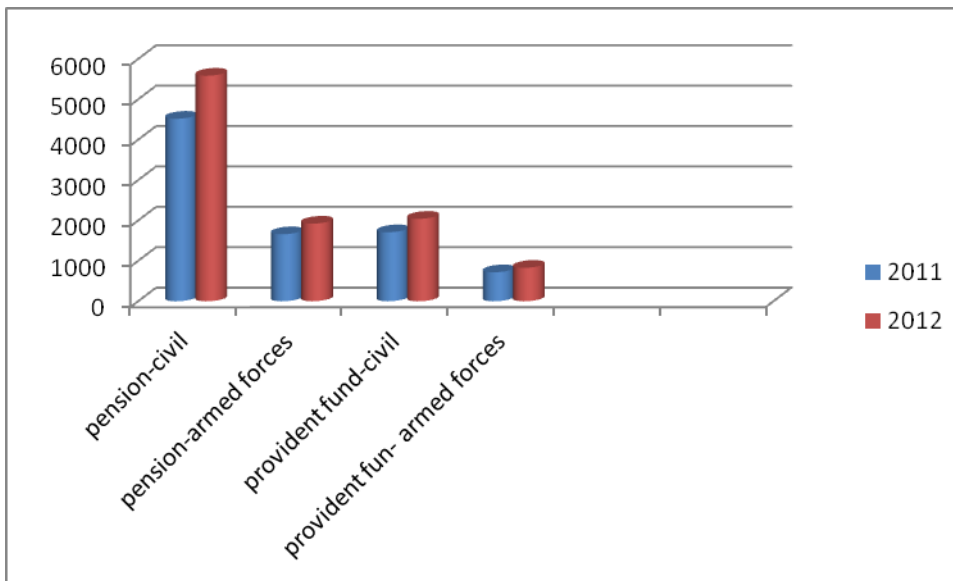
5. PENSION

NPPF is the government pension fund service provider in the country; the plan covers from retirement benefits, survivors' benefits to permanent disability benefit for its members. It covers the civil service and Government corporations which are designed on a Pay-As-You-Go partially funded system. From the total contributions by the members, 11 percent to provident fund and 11 to pension fund every month. As the pension fund is indexed to the Average Civil Service Salary Index, the benefit level increases with every increase in civil service salary.

Besides the civil pension, the NPPF also manages the Armed Forces pension scheme. The Armed Forces scheme covers the Royal Bhutan Army, Royal Body Guard and Royal Bhutan Police. The Armed Forces scheme is designed differently from the civil pension scheme in view of the different retirement age. For instance the service condition of the Armed Forces requires their personnel to retire at the age of 45 years whereas it is 56 years for the civil although it is also financed on a Pay-As-You-Go partially funded system.

Provident Fund provides the benefits in lump – sum to the retirees on superannuation and to the nominees in case of their death.

NPPF receives monthly inflow of fund from its members and invest those funds in the marketable securities and lending to sectors as approved by the RMA. NPPF provides Education and Housing Loan for its members.



Fund	2011	2012
Pension Fund - Civil	Nu.4, 520.87 million	Nu.5, 585.45 million
Pension Fund - Armed Force	Nu. 1,659.36 million	Nu.1,922.94 million
Provident Fund - Civil	Nu.1708.62 million	Nu. 2041.14 million
Provident Fund –Armed Force	Nu.717.09 million	Nu.827.47 million

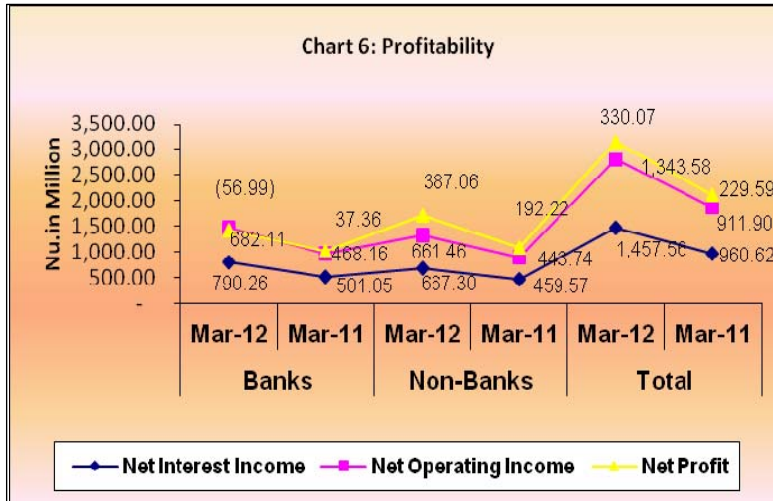
As of March 2012 the NPPF has made a total payment of Nu.10.54 million to 3094 beneficiaries which comprised of 1,317 normal pensioners, 458 early pensioners, and 6 disabled, 292 surviving spouse, 986 surviving children, 31 orphans and 4 dependent parents.

Beneficiaries	Number
Normal pensioners	1317
Early pensioners	458
Disabled	6
Surviving spouse	292
Surviving children	986
Orphans	31
Dependent parents	4
Total	3094

As of 31st March 2012 the total number of retirees is 3012.

Type of Pension	Civil	Armed Forces
Normal Pensioners	593	845
Early pensioners	148	341
Early Retirees awaiting pension benefits	692	324
Retired prior to 10 years of service	64	5
total	1497	1515

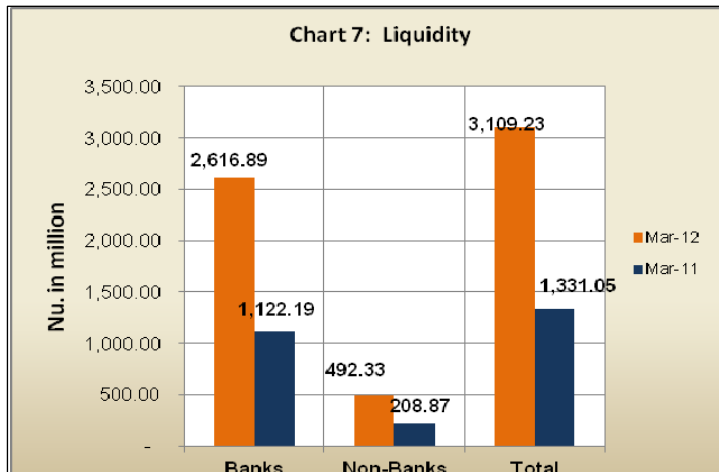
6. Profitability



The financial Institution during the quarter incurred a profit amounting to Nu. .33 billion from profit of Nu. .22 billion in March 2011. The increase in the net profits of the financial sector is mainly seen in the increase in the profit of non-banks, from Nu. .19 in March, 2011 to Nu. .38 billion in March, 2012. However, the banks suffered a net loss of Nu. .05 billion in March, 2012 from a profit of Nu. .03

billion in March, 2011. The incurring of loss is due to the requirement of high provisions kept for the non-performing loans. The net interest income of the banks rose to Nu.0.79 billion in March 2012 from Nu.0.50 billion in March 2011 or by 57.72 percent. Similarly, the net interest income of non-banks increased to Nu. .66 billion from Nu. .45 billion during the period under review.

7. Liquidity



The excess liquidity of the financial sector increased from Nu. 1.33 billion in March 2011 to Nu.3.10 billion in March 2012. The statutory liquidity requirement of the banks stood at 24.73 percent (4.73 percent above the regulatory requirement of 20 percent) as compared to 22.03 percent in March, 2011. The increase is due to increase in the quick assets of the banks by 12.28 percent (from Nu. 12.19 billion to Nu. 13.69 billion). Similarly, the non-banks' SLR position stood at 17.63 percent, 7.63 percent above the minimum prudential requirement of 10 percent. The quick assets of non-banks has increased by 48.84 percent (from Nu. .76 billion to Nu. 1.14 billion).