# FINANCIAL ANALYSIS

1. The financial analysis reviewed the financial position of Infrastructure Development Company Limited (IDCOL) in connection with the proposal to provide Bangladesh with a $526 million Asian Development Bank (ADB) multitranche financing facility for the Third Public–Private Infrastructure Development Facility (PPIDF 3). The analysis found that IDCOL, which will be the financial intermediary for PPIDF 3 has adequate financial resources and loan demand to support this ADB intervention.

## A. Background

2. IDCOL is a non-bank financial institution registered as a public limited company under the Companies Act 1994. It has policy mandate to participate as well as to promote participation of the private sector in investment and operation, ownership and maintenance of new infrastructure facilities in Bangladesh. It is the only domestic financial institution that can catalyze international long-term foreign currency funding and has the technical capacity to properly structure and execute infrastructure and project financing.

3. Based on audited financial statements as of 30 June 2015, IDCOL had total assets of Tk62.4 billion ($800 million), a loan book of Tk35.9 billion ($460 million), and paid-up capital of Tk3.85 billion ($49.2 million). It has 59 staff and a board composed of four members from the private sector, three government officials, and the company's managing director. IDCOL's funding sources include its equity capital, repayments from outstanding project finance loans, and refinancing funds provided by the development partners. About 70.0% of the company's loan portfolio is in the renewal energy sector, followed by the power (26.7%), telecommunications (1.7%), information technology and services (0.4%), ports (0.3%), and other sectors (1.0%).

4. IDCOL's strengths include stable liquidity and strong pre-tax earnings. The Credit Rating Agency of Bangladesh gave IDCOL a domestic rating of 'AAA' as of 31 December 2015. Table 1 summarizes IDCOL's key operating and financial highlights.

**Table 1: Infrastructure Development Company Limited—Financial Performance Highlights, FY2014–FY2015**

(Tk million)

| Audited Report Item | FY2014 | FY2015 |
|---|---|---|
| Total loans and advances | 29,115.0 | 35,973.0 |
| Total assets | 62,453.0 | 48,843.0 |
| Paid-up capital | 2,600.0 | 3,850.0 |
| Shareholder equity | 4,106.0 | 5,240.0 |
| Gross NPL | 232.0 | 569.0 |
| Gross NPL (%) | 0.8 | 1.6 |
| Return on equity (%) | 3.4 | 2.3 |
| Return on assets (%) | 3.0 | 2.1 |
| Debt–equity ratio (times) | 10.2 | 10.1 |
| Average cost of deposit and borrowing (%) | 2.8 | 2.7 |
| Equity–total liability ratio (times) | 9.2 | 9.2 |

FY = fiscal year, NPL = nonperforming loan.

Note: The fiscal year (FY) of the Government of Bangladesh ends on 30 June

Source: Infrastructure Development Company Limited annual reports.

## B. CAELS Analysis[1]

5. **Capital.** IDCOL's capital adequacy was found to be adequate. Its paid-up capital increased to Tk3,850 million during FY2015 from Tk2,600 million in FY2014 on the back of internal capital generation. The issuance of a bonus share of Tk1,150.0 million from the retained earnings was used to further raise the paid-up capital to Tk5,000 million at end of 2015.

6. The Basel II capital adequacy requirements have been implemented in the nonbank financial institution (NBFI) sector in Bangladesh since January 2012. Bangladesh Bank has issued prudential guidelines on capital adequacy and market discipline to promote international best practices and make the assessment of capital of NBFIs such as IDCOL more risk-based. NBFIs are required to maintain a minimum capital adequacy ratio of 10%, with at least 5.0% in core capital. IDCOL's capital adequacy ratio was 11.9% as of 30 June 2015, higher than 10.3% average for the banking industry overall.

**Table 2: Minimum Capital Requirement under Capital Adequacy and Market Discipline (As on 31 June, Tk. million)**

| Items | FY2012 | FY2013 | FY2014 | FY2015 |
|---|---|---|---|---|
| Tier 1 (core capital) | 2,235.0 | 3,479.0 | 4,740.0 | 5,453.0 |
| Tier 2 (supplementary capital) | 177.0 | 276.0 | 379.0 | 385.0 |
| **Total Eligible Capital** | **2,412.0** | **3,755.0** | **5,119.0** | **5,837.0** |
| Total risk weighted assets (RWA) | 18,630.0 | 35,250.0 | 38,210.0 | 49,140.0 |
| Capital adequacy ratio (%) | **12.9** | **10.7** | **13.4** | **11.9** |
| Tier 1 capital to RWA (%) | 12.0 | 9.9 | 12.4 | 11.1 |
| Tier 2 capital to RWA (%) | 0.9 | 0.8 | 1.0 | 0.8 |
| **Minimum Capital Requirement** | **1,863.0** | **3,525.0** | **38,210.0** | **4,917.0** |

Source: Infrastructure Development Company Limited.

7. **Asset quality.** Loans and advances are the major components of the asset composition of IDCOL. The company's loan portfolio grew by 24.0% in FY2015 at Tk35,973.0 million on account of strong advances made to renewable energy and infrastructure projects. Also, IDCOL's top 10 large loans outstanding exposures amounted to Tk29,949.0 million which account for 67.0% of its total loan portfolio. With IDCOL's high concentration on particular sectors and borrowers, vulnerability of assets to credit risks has also increased. Nevertheless, IDCOL's ratio of gross nonperforming loans (NPLs) to total loans and net NPLs to net total loans are only 1.6% and 0.2% in FY2015, respectively

8. Although these NPL ratios are lower than those of most banks and industry peers, IDCOL's non-performing loans are increasing which impact asset quality. Gross NPLs increased from Tk198.8 million in FY2014 to Tk568.5 million in FY2015.

**Table 3: Infrastructure Development Company Limited—Asset Quality Ratios, FY2013–FY2015**

| Item | FY2013 | FY2014 | FY2015 |
|---|---|---|---|
| Gross NPL (Tk million) | 198.8 | 232.3 | 568.5 |
| Gross NPL ratio (%) | 0.8 | 0.8 | 1.6 |

[1] CAEL stands for capital, asset quality, earnings, liquidity and sensitivity to market risk. It is a derivation of a common industry framework, the CAMELS analysis. The management component of the analysis was omitted because the Financial Management Assessment (as part of the linked documents) substantively addresses these issues.

| Item | FY2013 | FY2014 | FY2015 |
|---|---|---|---|
| Total provision held (Tk million) | 455.5 | 541.5 | 758.0 |
| Total provisions (% of total loan) | 1.9 | 1.9 | 2.1 |

FY = fiscal year, NPL = nonperforming loan.
Source: Infrastructure Development Company Limited annual reports.

9. IDCOL follows Bangladesh Bank's guidelines and rules on loan classification and provisioning (Tables 4 and 5).

**Table 4: Bangladesh Bank Guidelines on Classification and Provisioning for Loans with Tenors of 5 Years of Less**

| Overdue for | Category | Provision Requirement |
|---|---|---|
| < 3 months | Standard (S) | 1% |
| 3 to 6 months | Special Mention Account (SMA) | 5% |
| > 6 months but <=9 months | Substandard (SS) | 20% |
| > 9 months but <=12 months | Doubtful (D) | 50% |
| > 12 months | Bad/Loss (L) | 100% |

| | **For loan tenors > 5 years** | |
|---|---|---|
| **Overdue for** | **Category** | **Provision Requirement** |
| < 6 months | Standard (S) | 1% |
| 6 to 12 months | Special Mention Account (SMA) | 5% |
| >12 months but <=18 months | Substandard (SS) | 20% |
| > 18 months but <=24 months | Doubtful (D) | 50% |
| > 24 months | Bad/Loss (L) | 100% |

Source: Bangladesh Bank.

10. In FY2015, required provision for classified loans, i.e. substandard, doubtful, and loss accounts, was Tk248.0 million which was kept as specific provisions. Based on a rating report from Credit Rating Agency of Bangladesh (CRAB), IDCOL's pre-provision profit to net loans for assessing the company's ability to survive problems in the future was 7.5% in FY2015 (from 9.3% in FY2014), which indicates that 7.5% of currently performing loans can be written off without charging on reserves and equity.

11. ADB observed during its due diligence for the proposed facility that IDCOL's total rescheduled or restructured loans increased substantially from Tk1,500.0 million at end of FY2015 to Tk5,269.0 million at the end of FY2016.[2] This represented 15.0% of its total loan portfolio. Most of the restructured loans were for IDCOL's SHS program, which has shown negative growth since FY2013. Out of the 56 loans IDCOL made to participating organizations (POs) under its SHS program, loans to 2 of its POs amounting to Tk3,824.0 million have been rescheduled and 9.0% of all loans to its POs are classified loans in the substandard category[3] The classification of these loans has reduced IDCOL's overall profitability, since loans to the SHS program organizations account for 70.0% of its loan portfolio.

12. **Mitigating measures.** IDCOL has adopted a number of proactive measures to mitigate these risks such as pursuing the defaulting debtors through legal proceedings, increasing its debt recovery efforts, preparing detailed restructuring plans. It is carrying out a program to make

2 Loans can be restructured subject to approval by the central bank to accommodate a borrower in financial difficulty and thereby avoid a default.
3 As per the classification of Bangladesh Bank, classified loans in the substandard category are loans past overdue for 3 months or beyond but less than 6 months.

its collections under its SHS scheme more efficient. IDCOL has agreed to intensify these efforts by establishing a recovery unit under a new senior staff member to be engaged who will report to the head of IDCOL's credit management department. IDCOL will also strengthen its internal control and risk management capacity and process to ensure that sound financial management practices are in place. It will appoint a senior manager with background in risk management to head credit management and become a voting member of the company's credit risk management committee. It will engage an internal auditor at senior level to head its internal audit unit, which will report directly to IDCOL's board of directors. The appointment of these senior staff members will have to be completed prior to ADB loan effectiveness under tranche 1 of PPIDF 3.

13. **Earnings.** Though IDCOL experienced substantial growth by 24.0% in its loan portfolio in FY2015, its net interest income from loans and advances grew only moderately by 9.1% in FY2015 resulting from reduced yield on loans and loan restructuring and rescheduling efforts. Overall, earnings remain adequate with interest income mainly coming from income from advances made to renewable projects (80.0% of interest income) and infrastructure loans (20.0%).

14. IDCOL's profit before tax and provisions was Tk2,656 million in FY2015, 1.0% lower than Tk2,690.0 million in FY2014. The company's operating expenses grew by almost 26.0% due to the need to expand its organizational capacity (primarily staff resources) to support its business growth. Profitability has also been affected by the fact that income from IDCOL's SHS program showed negative growth during FY2013 to FY2015. This has been due to market saturation, a lack of regulation, and introduction of SHSs of lower quality than those provided by the IDCOL program that are now being offered in the market at a lower price. With the current 9.0% of total SHS loans in the substandard category, this also had an adverse effect on IDCOL's loan loss provisioning. IDCOL needs to continue to hold additional equity beyond the regulatory minimum in order to mitigate this risk.[4]

15. Subsector diversification somewhat mitigates IDCOL's portfolio concentration risk. IDCOL has added new business units and lending windows with increased focus on as energy efficiency, public–private partnerships, and advisory services. IDCOL has broadened its attention within its renewable energy activities toward investments in solar-based irrigation and solar-powered mini electricity grids. IDCOL's overall profitability has remained stable, and its net profit margin was 46.0% in FY2015 on the back of a sound cost structure. IDCOL maintained one of the lowest cost-to-income ratios in the industry and had a net interest margin of 5.0% in FY2015.

16. **Liquidity.** Due to its access to stable long-term funding through multilateral development institution loans, IDCOL is not dependent on short-term financing. In FY2015, 60.0% of its total funding came from the International Development Association and the World Bank, 25.0% from ADB, and 12.0% from the Japan International Cooperation Agency. The weighted average cost of funds was about 2.7%. IDCOL's operations generate sufficient cash flows to meet interest expenses. The ratio of earnings before interest, tax, depreciation, and amortization (EBITDA) to interest expense was 2.9 in FY2015 and indicates that IDCOL will be able to roll over its maturing debt.

---

[4] Risk Assessment and Risk Management Plan (accessible from the list of linked documents in Appendix 2 of the Report and Recommendation of the President). The plan describes IDCOL's problems with its SHS program and its measures to address the issues.

**Table 5: Infrastructure Development Company Limited—
Liquidity Profile, 30 June 2015**
(Tk million)

| Item | Up to 1 Month | 1–3 Months | 3–12 Months | 1–5 Years | Above 5 Years | Total |
|---|---|---|---|---|---|---|
| Assets | 1,791 | 17,850 | 19,651 | 19,583 | 3,577 | 62,453 |
| Liabilities | - | 187 | 3,846 | 13,960 | 39,214 | 57,213 |
| Net liquidity gap | 1,791 | 17,663 | 15,805 | 5,624 | (35,642) | 5,240 |
| Cumulative liquidity gap | 1,791 | 19,454 | 35,259 | 40,882 | 5,240 | |
| Gap as % of liability | - | 9,423 | 411 | 40.3 | (90.9) | 9.2 |

Source: Credit Rating Agency of Bangladesh.

17. IDCOL participates in call market operations and was a net lender throughout FY2015. Its liquidity profile shows a positive liquidity gap in all the buckets within 1 year. While the NBFIs in Bangladesh are allowed to mobilize term deposits only, term liabilities are subject to a statutory liquidity requirement of 5.0%, inclusive of an average 2.5% cash reserve ratio on bi-weekly basis. IDCOL is exempt from maintaining this statutory liquidity requirement because it is government-owned. IDCOL's total liquid assets were 38.0% of total assets and 45.0% of total deposits and borrowings at the end of FY2015.

18. **Sensitivity to risks.** IDCOL is exposed mainly to market, credit, and operational risks. Market risks arise from the potential for fluctuation of returns due to macroeconomic factors affecting the overall performance of the financial market and the company itself. Its asset liability management committee reviews the market trend of interest rates and matches the interest risks of assets so that it can meet its obligations without making any losses. This also ensures that IDCOL has adequate capital to cover potential losses from its exposure to changes in interest rates. IDCOL ensures that its lending and borrowing are in the same currency to avoid foreign currency risk.

19. IDCOL has adequate system for reporting of core risks of financial institutions issued by Bangladesh Bank on (i) credit risk management, (ii) internal control and compliance, (iii) asset–liability management, (iv) prevention of money laundering and terrorist financing, and (v) information and communication technology. ADB's technical assistance under the proposed PPIDF 3 will enhance IDCOL's institutional capacity by helping the company develop an integrated risk management framework. The framework will include a management information system to provide the data platform and analytics required for an infrastructure financing company to evaluate its performance and manage risks for reporting to its board.