Indicators of Project Business Success
for Financial Intermediaries

Project business success measures the project's impact on past and future performance of the FI's profitability and viability. Depending on the project size compared to the entire FI, sometimes it is hard to distinguish the project performance from the overall FI's performance. Nevertheless, irrespective of the type of MDB financing (general or targeted), the analytical overview should at least cover **CAMEL:**

Capital adequacy

Asset quality

Management quality

Earnings performance

Liquidity structure and balance sheet

Before starting the CAMEL analysis, following policies of the FI should be assessed:

- interest accrual policy,
- loan provisioning practices,
- maximum loan to deposit ratio and
- equity capital adequacy (as percent of total assets).

These policies should be in line with internationally accepted standards. Adjustments to the FI's profitability and capital adequacy should otherwise be made to reflect the application of these standards.

Capital Adequacy

- Analyze CAR level, trends throughout project life and prospects for near future; compare with peers.
- Identify systemic risks related to CAR.
- Analyze quality of capital (share of tier I, tier II and tier III capital).
- Assess if CAR adjustments are needed due to: low level of provisioning, risk weightings (e.g. zero weight for government securities could be an issue), intangibles, deferred taxes, derivatives and off-balance sheet commitments.

Asset Quality

Breakdown by earning assets and review of their credit quality:

– Loans[1]:

- Total loans' amount, % of total assets, growth trends vs. peers and macroeconomic conditions.
- Identify any systemic risks (including issues with legal regulations) related to the loan portfolio quality.
- Loan concentration by single client, group, related party exposure (on and off-Balance Sheet), type of borrowers (public, commercial, retail, housing, etc.), sector, currency, etc.
- NPLs – level and trend of NPLs over the project life, including the basis for NPL classification (e.g. NPLs covering principal in arrears and principal outstanding for loans past due over 90 days), particularly high exposure to any sector or borrower; FI's efforts to reduce NPLs.
- Provisions – assess the adequacy of the level of provisions (following the NPLs breakdown by category: e.g.: watch, doubtful, substandard, loss). Analyze if provisions cover NPLs only or past due interest as well.
- Open loan exposure – level and trend over project life and factors affecting the changes (e.g. increased equity may artificially reduce the open loan exposure).

– Fixed income securities;

– Equity securities;

– Off-Balance Sheet items.

Management Quality

- Expertise and experience;
- Strategic vision;
- Corporate governance;
- Ownership structure;
- Organizational structure;
- Staff – training, knowledge, compensation.

Earnings Performance

- Profitability Ratios: ROAE, ROAA, net income, net interest margin (when applicable) – level, trends; factors affecting, peer comparisons.
- Income stability: analyze net interest income (from loans; securities; interbank) vs. non-interest income (fee and commission; FX gains, securities trading gains); provisions, operating expenses. Trend and share of interest receivable.
- Provision burden (provisions/net interest income).
- Extraordinary items.

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[1] Indicators of declining loan quality: excessive growth, especially if already high generation; high concentration, related party lending, weak credit procedures, poor pricing, restructurings.

- Efficiency ratios: cost/income ratio[2] and/or cost/assets ratio– level, trends and peer comparisons.
- Analyze FI stock performance, if listed, and issues that are affecting the stock market performance.

Liquidity and Balance Sheet

- Size of assets, trends, breakdown by group of assets (minimum risk; trading; investments; loans; others)[3]; extent of exposure to the government and state owned enterprises, with description of risks for the largest exposures.
- Funding diversity and stability – sources of funding, their size and trends, breakdown by class with description of potential risks (e.g. share of short term funding; cost of funding vs. market average; type, term and volatility of deposits; deposit concentration ratio), reliance on one source of funding.
- Maturity mismatch ratio for 1 or 3 months. Identify existing or potential liquidity risks and any related mitigating factors.
- FX risk (open foreign exchange exposure risk).
- Interest rate risk.

[2] Cost/income=non interest expenses, excluding loan loss provisions/ (net interest income plus non-interest income)

[3] Minimum risk assets include cash and inter-bank deposits. Trading assets include securities (trading book), reverse repos, derivatives (mark to market gain). Investments include securities (held for sale and to maturity), associates. Other includes other real estate owned, foreclosed assets, accrued interest income.