ICRA Lanka assigns "[SL]A-" rating for the proposed Senior unsecured redeemable debenture programme of Commercial Leasing and Finance PLC

May 27, 2015

Instrument	Amount	Rating Action
Senior Unsecured Redeemable Debentures	LKR 5,000 Mn	[SL]A- assigned with stable outlook

ICRA Lanka has assigned the [SL]A- (pronounced S L A minus)rating with a stable outlook for the proposed senior unsecured redeemable debenture programme amounting to LKR 5,000Mn of Commercial Leasing and Finance Company PLC (CLC or the Company). ICRA Lanka also has an issuer rating of [SL]A-(Stable) outstanding on CLC. Given the significant operational and financial linkages with the Holding company (Holdco; Lanka Orix Leasing Company PLC), ICRA Lanka continues to take a consolidated rating view of the HoldCo and the key asset financing subsidiaries.

At group level, the rating factors in LOLC Group's long track record and established position in the retail finance sector, professional and experienced management team and adequate risk management systems with a strong retail franchise. The rating also derives support from the committed support and oversight from its Key investor of the Holdco–ORIX Corporation of Japan (rated Baa2 with stable outlook by Moody's), which has a 30% stake in the entity. The Group's performance is largely dependent on its key financial service subsidiaries due to the modest contribution from the non-financial service subsidiaries. At group level it would be important to further improve the overall asset quality of the key financial services subsidiaries, by controlling incremental slippages and focused recovery initiatives going forward.

At company level, ICRA Lanka factors in CLC's demonstrated track record of operating profitably in the retail finance segment, its well established franchise combined with a professional and experienced management team, improvement in profitability indicators and comfortable capitalization levels. The company's liquidity profile is expected to remain comfortable, notwithstanding the gaps observed in the short term buckets, in the recent past. The company has a good asset quality profile as compared to most peers; ability of the company to restrict incremental slippages would be a key rating sensitivity from a credit perspective.

CLC's recorded 10% (annualized) growth in its overall portfolio for the 9MFY2015; similar to the growth reported in FY2014. The portfolio's asset quality registered improvement during the 9M driven mainly by moderation in overall slippages. CLC's reported Gross NPA ratio as at Dec-14 was 2.18% down from 3.03% as at Jun-14 (2.38% - Mar-14) due to both recoveries and write offs carried out during the period. CLC's NPA provisioning level is comfortable at 73% in December 2014, notwithstanding moderation from 167% in March 2014.

During 9MFY2015 CLC acquired about 59% of BRAC Lanka Finance PLC (BRAC) directly and acquired additional 35% from LOLC Micro Investments Limited, a Group Company; thus giving CLC an ownership of 94% of BRAC as in Dec-14, and subsequently made a mandatory offer to acquire all remaining shares of BRAC. The acquisition has not impacted the financial risk profile of the company. CLC's capitalization levels remained strong with Regulatory Total Capital Adequacy Ratio reported at 22.5% (Tier-I at 25.3%) and gearing at 2.73 times as in Dec-14.

CLC's shorter term ALM (Asset-Liability Maturity) mismatches had widened during 9MFY2015. The main reason for this is the accelerated pace of mobilizing fixed deposits (mostly shorter term). ICRA Lanka however takes note of the good renewal rates of around 60% of the fixed deposits and, further the proposed debenture issue is likely to temper the mismatches as business growth is expected to remain moderate in the next 3-6 months.

CLC's overall profitability levels for 9MFY2015 has improved compared to FY2014 mainly due to an improvement in the lending spreads. The company has been able to re-finance its shorter term borrowings at lower rates taking advantage of the declining interest rate environment during CY2014, leading to considerable reduction in overall cost of funds. Decrease in provisioning costs resulting from some moderation in the incremental slippages and reduction in the provision cover supported CLC's profitability indicators. Consequently, CLC's Return on Average Assets (RoAA) improved to 4.5% for 9MFY2015 (annualized) as compared to 3.1% in FY2014 and Return on Average Net Worth for 9MFY2015 (annualized) improved to 17.16% compared to 11.21% for FY2014. Although the company is likely to improve its provision cover going forward, ICRA Lanka expects the company to maintain a healthy RoAA of 3.8-3.9% going forward.

Company Profile

CLC was incorporated in the year 1988 as a Specialised Leasing Company. LOLC Group acquired controlling stake and then 100% of the company in 2008. The main product lines of CLC include leasing, hire purchase and loans for vehicles and equipment and, factoring. CLC obtained the license to operate as a LFC in December 2011. Subsequently, CLC has also started offering savings and deposit products. CLC operates primarily in the SME and Micro Sectors. Business is mostly sourced by third-party Agents/brokers, but the company has managed to maintain a strict control over originations standards. CLC was relisted in the Colombo Stock Exchange (CSE) on June 05, 2012 to comply with the requirements of the Central Bank of Sri Lanka (CBSL).

For the nine month period ended December 2014, CLC reported a net profit of Rs. 1,223 million on a total income of Rs. 6.1 billion compared to net profit of Rs. 936 Million on a total income of Rs. 7.7 billion in FY2014.

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