ICRA Lanka reaffirms the issuer rating of [SL]BB+ and issue rating of [SL]A-(SO) of Orient Finance PLC

August 09, 2017

Instrument	Amount	Rating Action
Issuer	N/A	[SL]BB+ with stable outlook reaffirmed
Guaranteed Redeemable Debentures Programme	LKR 1,000 Million	[SL]A-(SO) with stable outlook reaffirmed

ICRA Lanka Limited, Subsidiary of ICRA Limited, group company of Moody's Investors Service, has reaffirmed the issuer rating of **[SL]BB+ (Pronounced SL double B plus)** with a stable outlook to Orient Finance PLC (OFP or the Company). ICRA Lanka has also reaffirmed the rating of **[SL]A-(SO) (Pronounced SL A minus Structured Obligation)** with a stable outlook to the LKR 1,000 Mn Rated Guaranteed Redeemable Debentures programme. The letters SO in parenthesis suffixed to a rating symbol stand for Structured Obligation. An SO rating is specific to the rated issue, its terms, and its structure. The SO rating does not represent ICRA Lanka's opinion on the general credit quality of the issuer concerned.

The issuer rating draws comfort from the financial, managerial and operational support available from the Janashakthi group, its experienced board and senior management team. The rating also factors the improvement in asset quality (gross NPA 5.5% in March 2017 vis-à-vis 7.8% in March 2016), due to strengthened credit evaluations and recovery efforts by the company. The rating, however, is constrained by OFP' moderate capitalization (total CAR of 11.7%% in March 2017 and 8.9% in March 2016) and subdued profitability indicators (PBT/ATA[1] for FY2017 at 1.7% and 1.9% in FY2016). The issuer rating further takes note of the recent regulatory restrictions on vehicle financing, further intensifying the competitive vehicle leasing business in Sri Lanka. The above is expected to exert pressure on portfolio growth and lending margins for players in the segment, including OFP. In the light of these developments, OFP's ability to control credit cost and operating expenses, would be critical for incremental profitability. The company's funding profile continues to be dominated by fixed deposits; the same has moderated recently (58% of the total debt as in March 2017 vis-à-vis 64% in March 2016), as the company has been able somewhat diversify its funding base through long term bank borrowings.

The rating for the LKR 1,000 Mn Guaranteed Redeemable Debentures programme is based on the strength of an unconditional and irrevocable guarantee from Janashakthi Insurance Company PLC (JIP/the Guarantor) to the extent of the entire principal and two interest instalments, and the payment mechanism designed to ensure repayment of the rated instrument even if OFP does not pay and the guarantee has to be invoked by the debenture trustee. The rating also assumes that the guarantee will be duly invoked by the debenture trustee, as per the terms of the underlying transaction, in case there is a default in payment by OFP. ICRA Lanka has a claims paying ability rating of [SL]A (pronounced SL A) with stable outlook outstanding on Janashakthi Insurance PLC. Please refer to our detailed rationale dated July 25, 2017 for the same.

OFP is a mid-sized NBFC with a portfolio of about LKR 17.1 Bn as on March 31, 2017. The company was formed post the merger of the "Erstwhile OFP" with Bartleet Finance PLC (BFP) in Ju1y 2015, post which BFP was renamed as Orient Finance PLC. Close to 77% of the portfolio is backed with vehicle financing with about 9% towards factoring and about 10% towards equipment finance as in

[1] Profit before tax/ average total assets (Excluding onetime gains and extraordinary income)

March 2017. In terms of asset classes, about 27% of the portfolio is towards commercial vehicle and tractor financing, with 22% being towards car/vans, 24% towards 3-wheeler and about 4% towards 2-wheelers. Overall portfolio growth has moderated to 16% in FY2017 vis-à-vis 28% in FY2016, largely because of the change in the regulations for leasing, which came into effect during the last quarter of the financing year. Despite the moderate growth outlook, OFP intends to focus on its core vehicle leasing business. Going forward, the company plans to grow at a moderate rate of about 15%-20%, over the near – medium term. Ability to register optimal growth and good business margins would be crucial given the competitive operating environment.

The rating takes cognizance of recent improvements in overall asset quality, where the gross NPA has reduced to 5.5% in March 2017 vis-à-vis 7.8% March 2016 and 11.4% in March 2015; absolute gross NPAs have also reduced to LKR 929 Mn in March 2017 vis-à-vis 1,113 Mn in March 2016. Tight credit evaluation, collection and recovery processes has resulted in the overall improvement in asset quality. Going forward, OFP's ability to maintain slippage and manage the recovery of legacy portfolios will be crucial, from a rating point of view.

OFP's capitalization profile is moderate with core capital adequacy at 9.0% and overall capital adequacy ratio at 11.7% as on March 31, 2017 (core CAR at 8.9% and total CAR at 9.6% in March 2016). During FY2017, tier 2 capital base of the company was enhanced by the issue of LKR 400Mn, redeemable preference shares, which was subscribed by Janashakthi PLC. Reported gearing was 6.4x in March 2017 (6.2x in March 2016), while gearing adjusted for revaluation reserves and goodwill stood at a high 8.8x in March 2017. The company' ability to have a risk adjusted capital structure going forward in relation to the growth plans and adequate internal generation would be crucial from a rating perspective.

OFP's funding profile is characterised by deposits which constituted about 58% of the total borrowings as in March 2017 (about 64% in March 2016), while funding from banks, debentures and securitizations accounted for the rest. ICRA Lanka notes the efforts taken by the company to diversify the funding structure by taking on more long term bank borrowings and reduce the deposit concentration by expanding the retail deposit base. Due to these efforts, OFP's <1 year ALM mismatch has improved to 17.4% as in March 2017 vis-à-vis 27.5% in March 2016. The company enjoys deposit renewal rate of about 70-75% and has unutilized funding lines close to LKR 2.0 Bn as on June 30, 2017 which supports in liquidity profile.

Notwithstanding the sharp increase in deposit rates, OFP has been able to maintain its lending margins (NIM in FY2017 was 7.1% vis-à-vis 7.3% in FY2016), due to prudent funding strategies employed by the company. Credit cost has improved (credit provisions/ATA was 1.8% in FY2017 vis-à-vis 2.1% in FY2016) on account of improvement in the asset quality indicators. Operating expenses/ATA stood at 4.6% in FY2017, compared to 4.1% during the previous fiscal, while PBT/ATA was 1.7% in FY2017 vis-à-vis 1.9% in FY2016. Going forward, the improvement in overall profitability will have to come from improved credit costs and operational efficiencies, as the room for expanding lending margins is likely to be limited because of competitive pressures.

Company Profile

Orient Finance PLC (formerly known as Bartleet Finance PLC prior to the merger) was incorporated in 1981. The Company is a registered finance company and was licensed by the Monetary Board of Sri Lanka to accept Fixed Deposits from the public. The Company was listed on the Main Board of the Colombo Stock Exchange in June 2011.

In July 2015, BFP acquired erstwhile Orient Finance Plc after paying close to LKR 1.70 Bn in cash and 1,213 Bartleet shares to the OFP shareholders. After the merger, the company was renamed as Orient Finance PLC and Janashakthi PLC became the main shareholder of the company with a 99.9% shareholding. In January 2015, OFP made an initial public offer (IPO) of about LKR 1.0 Bn. Objective of the IPO was to improve the capital structure of the company and settle the short term loan obtained from Orient Capital Limited (a fully owned sub-subsidiary of Janashakthi PLC) for acquisition. Currently Janashakthi PLC holds about 89.8% of the shareholding of OFP.

For FY2017, OFP reported a PAT of LKR 265 Mn on a total asset base LKR 18.3 Bn, compared to PAT of LKR 607 Mn (including the tax credit of LKR 311 Mn) on a total asset base of LKR 15.5 Bn during the corresponding period, previous fiscal.

Parent Profile – Janashakthi PLC

Janashakthi PLC (JP) is an Investment holding company incorporated in the early 1990's. The company is an investment holding company of the Schaffter family. The main subsidiary of JP is Janashakthi Insurance PLC which is an established insurance company in Sri Lanka operating for over two decades. Presently Orient Finance PLC has become the other significant subsidiary of the company. Janashakthi PLC is jointly owned by Prakash Schaffter (49.99%) and Ramesh Schaffter (49.99%), sons of Mr. Chandra Schaffter.

For the 9M ended December 31, 2016 Janashakthi PLC reported a standalone loss of LKR 561 Mn on a total income of LKR 146 Mn, compared to the loss of LKR 303 Mn on a total income of LKR 227 Mn during the corresponding period, previous fiscal. For the 9M ended December 31, 2016 Janashakthi PLC reported a consolidated PAT of LKR 335 Mn on a total income of LKR 12.9 Bn, compared to the consolidated PAT of LKR 1,128 Mn (including the LKR 524 Mn profit from disposal of subsidiary) on a consolidated total income of LKR 9.9 Bn during the corresponding period, previous fiscal.

Guarantor Profile – Janashakthi Insurance PLC

Janashakthi Insurance PLC was initially incorporated in Sri Lanka as Janashakthi Life Insurance Co. Ltd (Janashakthi Life), a public company with limited liability in 1992. JIP began its operations in September 1994, as Sri Lanka's first specialized life insurer and ventured into Non-Life Insurance through Janashakthi General Insurance Co Ltd (Janashakthi General), which was established in 1995. JIP and Janashakthi General were merged in 2000 to form JIP. JIP acquired National Insurance Corporation Ltd in 2001, and later diversified into other areas of financial services. JIP was the 3rd largest general insurer and 7th largest life insurer in Sri Lanka in Dec-15. Janashakthi General Insurance Limited (JGIL) was incorporated as a wholly owned subsidiary of JIP during 2014 and, JIP transferred the non-life business to JGIL from January 01, 2015, thus complying with the regulatory requirement. JIP fully acquired AIA General Insurance Lanka Limited during 2015 and merged it with JGIL during January 2016.

During the year ended December 2016, JIP reported a consolidated net profit of LKR 1,647 Mn on a gross written premium of LKR 13,651 Mn, compared to the net profit of LKR 951 Mn on a gross written premium of LKR 10,664 Mn for the 12 month ended December 2015. During the 3M ended March 2017, JIP reported a consolidated net profit of LKR 217 Mn on a gross written premium of LKR 3,789 Mn.

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