

ICRA Lanka assigns [SL]A-(Stable) issuer rating with stable outlook to First Capital Treasuries Limited; subordinated debentures rated at [SL]BBB+ with a stable outlook

September 11, 2015

Instrument	Amount	Rating Action
Issuer Rating	n/a	[SL]A-; assigned with stable Outlook
Subordinated Unsecured redeemable Debenture programme	LKR 500 Mn	[SL]BBB+; assigned with stable Outlook

ICRA Lanka has assigned the Issuer rating of [SL]A- (pronounced SL A minus) with a stable outlook to First Capital Treasuries Limited (FCTL or the company). ICRA Lanka has also assigned the [SL]BBB+ (pronounced SL triple B plus) rating with stable outlook to the LKR 500 Mn Subordinated Unsecured redeemable Debenture programme of the company.

The ratings factor in FCTL's position as an established Standalone Primary Dealer in Sri Lanka with a long track record, established franchise and clientele. The rating also factors in the prudent internal control and processes, along with the adequate risk management systems put in place, which is commensurate in relation to the risks intrinsic to a Primary Dealer's business. The ratings also factor in FCTL's comfortable liquidity position due to liquid nature of the portfolio and availability of sanctioned bank facilities. ICRA Lanka notes that while the portfolio of the company has minimal credit risk, the same however is susceptible to adverse movements in the interest rates. The rating takes note of the improvement in the financial performance of the company during FY2015, due to favourable interest rate scenario, which resulted in trading gains for the company; however the same is likely to moderate in the current financial year as the market interest rates are likely to remain largely range-bound or move upwards. In the above context, ICRA Lanka also notes that FCTL's portfolio duration, which had remained largely conservative in the past increased to 3.7 in March 2015 (3.2 in June 2015); this is likely to make its profits susceptible to unfavourable interest rate movements, if the same occurs within a short time span. Nevertheless, FCTL's established risk management system, its experienced dealing team and, its investment committee, which largely consists of the senior management and Board of Directors, reviews the various risks regularly thus mitigating risks to an extent. ICRA Lanka notes that the company's regulatory capital adequacy is comfortable at 21.8% as in March 2015 vis a vis the regulatory requirement of 8%; however FCTL's gearing has generally been higher than the industry average and, stood at about 10.2 times in March 2015 (5.9 times in June 2015) The company's regulatory capitalization is comfortable to absorb the losses, if any, on the current portfolio due to unfavorable interest rate movements. ICRA Lanka further notes that there is scope for FCTL in improving its effective participation in the primary market; trading gains in FY2015 was largely from the secondary market transactions. Further, the ratings take cognisance and would closely monitor the developments on the outstanding contingent liabilities (Tax demands), which stood at about 20% of the net-worth as in March 2015.

FCTL's portfolio as in March 2015 stood at about LKR 16 Billion, the same reduced to about LKR 10 Billion in June 2015 as the company brought down its portfolio holdings as the interest rate scenario is likely to remain largely range-bound or move upwards going forward, in the current financial year. The portfolio consists of Treasury bills and bonds, which do not carry credit risk and are highly liquid assets. The company is expected to deal only with government securities going forward also. However, FCTL is exposed to the counter party risks on its reverse repo exposures which were largely concentrated to about 7-8 entities as in March 2015. The company however closely

monitors its exposures and takes proactive measures to mitigate the impact of the above mentioned risks. ICRA Lanka however notes that the company has an established clientele and had undertaken transactions with more than 50 entities during the year apart from the retail participants. The company also has access to over 2500 clients of the First Capital Group (First Capital Holdings PLC and its subsidiaries). The First Capital Group entities have interests in margin trading, stock broking, asset management, corporate debt structuring and other investments banking activities. The size of these group entities presently however is quite modest in relation to FCTL.

During FY2015, the company's overall profitability improved as trading income increased sharply from LKR 227 Mn in FY2014 to LKR 900 Mn, while interest income remained largely stable. The above support the improvement in the overall profits of the company during the year as the operating expenses increased on account of bonus payments to employees. Consequently, FCTL's PAT as a proportion of average assets improved to 5.1% in FY2015 from about 4.2% in FY2014. ICRA Lanka notes the company's profitability performance in the current financial year is expected to moderate as trading gains are likely to be lower than in FY2015. FCTL's portfolio consists of highly liquid assets, which along with the sanctioned bank lines of about LKR 1 billion with the First Capital Group provides comfort from a liquidity perspective.

Company Profile

Incorporated in the year 1982, FCTL is a Licensed Primary Dealer in Sri Lanka. The company is 94.4% held by First Capital Limited, while First Capital Limited is in-turn 99.9% held by First Capital Holdings PLC. First Capital Holdings PLC is 74.9% held by Dunamis Capital PLC, which is the ultimate parent of FCTL.

During FY2015, FCTL reported a net profit of LKR 730 Mn on a total asset base of LKR 16,096 Mn vis a vis a net profit of LKR 518 Mn on a total asset base of LKR 12,552 Mn.

In the three months ended June 2015, the company reported a net profit of LKR 107 Mn on a total asset base of LKR 10,630 Mn.

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For further details please contact:

Analyst Contacts:

Mr. Karthik Srinivasan, (Tel No. +91-22-6114 3444)
karthiks@icraindia.com

Relationship Contacts:

Mr. W. Don Barnabas, (Tel. No. +94-11-4339907)
wdbarnabas@icralanka.com





Subsidiary of

ICRA Limited

A Group Company of Moody's Investors Service

CORPORATE OFFICE

Level 10, East Tower, World Trade Center, Colombo 01, Sri Lanka

Tel: +94 11 4339907; Fax: +94 11 2333307

Email: info@icralanka.com; Website: www.icralanka.com

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