

ICRA Lanka reaffirms the [SL]BBB- rating of Prime Finance PLC

March 03, 2020

Instrument*	Previous Rated Amount (LKR Mn)	Current Rated Amount (LKR Mn)	Rating Action
Issuer rating	N/A	N/A	[SL]BBB- (Stable); reaffirmed

Rating action

ICRA Lanka Limited, subsidiary of ICRA Limited, a group company of Moody's Investors Service, has reaffirmed the issuer rating of [SL]BBB- (Pronounced SL triple B minus) with Stable outlook of Prime Finance PLC (PRIM or the Company).

Rationale

The rating continues to factor in the financial, operational and management support from the Prime group; Prime Lands Private Limited rated [SL] A- (Stable) holds about 95% stake in PRIM. The rating also takes into consideration, PRIM's modest scale, its less seasoned portfolio, and subdued profitability indicators. The rating also takes cognizance of the recent deterioration of asset quality indicators of the Company, largely on account of challenging macro conditions that prevailed during the period. ICRA Lanka notes that the Company's current core capital, which stood at about LKR 1.6 Bn as in September 2019, is below the regulatory minimum of LKR 2 Bn. ICRA Lanka, however, factors the recent stock exchange filing for the rights issue to raise LKR 527 Mn fresh capital and the commitment from the parent company to extend capital and liquidity support to PRIM when required. Going forward, the Company's ability to raise the additional capital in a timely manner and its ability to improve overall asset quality indicators would be crucial from a rating point of view.

Outlook: Stable

The Stable outlook factors in the timely overall support from the Prime group. The outlook may be revised to "Positive" based on PRIM's ability to grow its portfolio and improve its earnings profile and asset quality indicators, while maintaining a healthy capital profile. The outlook may be revised to "Negative" in case PRIM is unable to meet the regulatory capital requirement in a timely manner or in case of a significant deterioration in its financial risk profile or lower than expected support from the Prime group.

Key rating drivers

Credit strengths:

Support from Prime group: The current promoter of the Company, Prime Lands (Pvt) Ltd (rated A- with Stable outlook) is the leading residential property developer in Sri Lanka. The promoter has demonstrated its ability and willingness to infuse needed capital for PRIM; during the CY2018, the parent infused a total of LKR 1.14 Bn in fresh capital through consecutive rights issues. Going forward, given PRIM's product focus on property-backed lending and other operational synergies, ICRA Lanka expects the support from the parent to be forthcoming.

Higher exposure to asset-backed lending: As in September 2019, PRIM's portfolio almost entirely consisted of asset-backed lending through real estate backed loans and vehicle leasing; real estate backed exposure accounted for over 70% of the total portfolio, while vehicle leasing accounted for the balance.

Credit challenges

Small scale of operations and relatively unseasoned portfolio: PRIM is a relatively small player in the NBFI industry with a portfolio of about LKR 4.5 Bn as in September 2019. Since the acquisition by the Prime Group in January 2017, the Company has aggressively grown its real estate backed lending portfolio, by exploiting the synergies with the parent group. ICRA Lanka notes that the average tenure of these products is about five years, and the portfolio remains relatively new and unseasoned up to now. PRIM's ability to grow its portfolio while maintaining healthy asset quality indicators will be crucial, going forward.

Shortfall in regulatory minimum capital, however, the parent company is expected to provide capital support in the immediate to short term: As in March 2019, adjusted core capital position of PRIM stood at about LKR 1.59 Bn (LKR 1.66 Bn un-audited as in September 2019), which is about LKR 400 Mn below the minimum capital requirement of LKR 2 Bn as of January 2020, as stipulated by the Central Bank of Sri Lanka (CBSL). In addition, the Company has to meet the LKR 2.5 Bn minimum capital hurdle that is set for January 2021. However, recently, PRIM has obtained approval from the CBSL to infuse LKR 527 Mn via a rights issue and the same is expected to be completed by June 2020; the Company is expected to satisfy the LKR 2 Bn minimal core capital requirement upon completing this capital raising exercise. Further, ICRA Lanka takes comfort from the commitment given by the parent company to provide capital support for the NBFI; timely completion of the proposed capital infusion plan will be a key monitorable, going forward.

Deterioration of asset quality indicators: During the 1H of FY2020, PRIM witnessed a sharp increase in NPA numbers, where gross NPA stood at about 9.8% in September 2019 vis-à-vis 5.5% reported in March 2019 (gross NPA about 7.3% in March 2018); 90+ DPD increase to 23.9% in September 2019 (15.2% March 2019). Higher slippages in working capital financing and the leasing portfolio along with the slippages in the property-mortgage loans largely contributed to the increased gross NPA ratio during the period. However, ICRA Lanka notes, that the increase in NPA is primarily attributable to the challenging macro-political environment witnessed during the period, and is largely in-line with the movement of systemic NPA levels.

Analytical approach: For arriving at the ratings, ICRA Lanka has applied its rating methodologies as indicated below.

Links to applicable criteria: [ICRA Lanka Credit Rating Methodology for Non-Banking Finance Companies](#)

About the Company:

Prime Finance PLC (PRIM), a registered finance company, is largely focusing on mortgage backed loans and leasing. PRIM was established in 2004 as Asia Commerce Limited and was registered as a finance leasing establishment in 2005. In 2011, the Company was registered under the Finance Companies Act and was rebranded as Divasa Finance Limited. The Company went through a name change in 2012 as George Stuart Finance Limited and listed on the Colombo Stock Exchange by way of an Introduction. Under the financial sector consolidation programme of the Central Bank of Sri Lanka, the Company was acquired by Sarvodaya Development Finance Limited (formerly known as Deshodaya Development Finance Company Ltd) in 2014 and changed the name of the Company to Summit Finance PLC in 2016. The current

shareholders, Prime Lands (Pvt) Ltd. acquired the Company in January 2017 and later changed the name to Prime Finance PLC. Prime Lands (Pvt) Ltd. presently holds 95% of PRIM.

During the year ended March 31, 2019, PRIM reported a net profit of LKR 179 Mn on a total asset base of LKR 5.7 Bn as compared to the net profit of LKR 13 Mn on a total asset base of LKR 3.7 Bn in the previous fiscal year.

For the six months ended September 30, 2019, PRIM reported a net profit of LKR 40 Mn (unaudited) on a total asset base of LKR 5.8 Bn.

Key financial indicators (Audited)

	FY2018	FY2019	6MFY2020*
Net Interest Income	236	539	276
Profit after Tax	13	179	40
Net worth	613	1,621	1,661
Loans and Advances	2,681	4,305	4,588
Total Assets	3,671	5,706	5,800
Return on Equity	2.8%	15.9%	4.9%
Return on Assets	0.5%	3.8%	1.4%
Gross NPA	7.3%	5.5%	9.8%
Core Capital Adequacy Ratio	21.0%	24.5%	24.8%
Total Capital Adequacy Ratio	21.0%	25.3%	25.9%
Gearing (times)	4.6	2.2	2.1

*Unaudited

Rating history for last three years:

Instrument	Current Rating (FY2020)		Chronology of Rating History for the past 3 years		
	Amount Rated (LKR Mn)	Date & Rating	Date & Rating in FY2019	Date & Rating in FY2018	Date & Rating in FY2017
Issuer rating	N/A	Feb 2020 [SL]BBB- (Stable)	Sep 2018 [SL]BBB- (Stable)	- N/A	- N/A

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