

## ICRA Lanka reaffirms the long term ratings of First Capital Treasuries PLC

October 4, 2016

Instrument	Amount	Rating Action
Issuer Rating	N/A	[SL]A- with Stable Outlook, Reaffirmed
Subordinated Unsecured Redeemable Debentures	LKR 500Mn	[SL]BBB+ with Stable Outlook, Reaffirmed

ICRA Lanka Limited, subsidiary of ICRA Limited, a group company of Moody's Investors Service, has reaffirmed the issuer rating of [SL]A- (pronounced SL A minus) with stable outlook for First Capital Treasuries PLC (FCT or the company). ICRA Lanka has also reaffirmed the issue rating of [SL]BBB+ (pronounced SL triple B plus) with stable outlook for the LKR 500Mn subordinated unsecured redeemable debenture programme of the company.

The ratings continue to factor in FCT's position as one of the leading standalone primary dealer in Sri Lanka with a long track record and its established franchise and clientele. The ratings also factor in the prudent internal control and processes, along with adequate risk management systems put in place, which is commensurate in relation to the risks intrinsic to a primary dealer's business. ICRA Lanka notes that while the portfolio of the company has minimal credit risk, the same however is susceptible to adverse movements in interest rates. The profitability was impacted during FY2016 due to the adverse interest rate regime which prevailed during the latter part of the fiscal. Going forward, company is expected to manage the risk of potential interest rate movements by maintaining portfolio durations at relatively lower levels compared to the recent past (weighted average portfolio duration as on June 30, 2016 was 1.8 years vis a vis 3.1 years in December 31, 2015). ICRA Lanka notes that while regulatory capital adequacy ratio stood at 19.2% as on June 30, 2016 as against the regulatory minimum of 10%, the gearing is very high at 17.1 times as on June 30, 2016 (9.6 times as on March 31, 2016). ICRA Lanka is also cognizant of the liquidity risk stemming from the high leverage and significant short term asset and liability mismatch, as the investment positions are largely funded by short term repo borrowings (94% of the borrowings as on June 30, 2016); liquid nature of the portfolio and availability of sanctioned bank facilities however provides comfort. Going forward, ICRA Lanka will closely monitor the gearing and liquidity profile of FCT, as they are key rating sensitivities for the company.

FCT's portfolio as on June 30, 2016 stood at about LKR 26 Bn. The same had increased substantially from LKR 15 Bn on March 31, 2016, as the company is aggressively pursuing the net interest income opportunity prevailing in the current market. 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, FCT is exposed to counter party risks on its reverse repo exposures which are fairly concentrated; the company however closely monitors its exposures and takes proactive measures to mitigate the impact of the above mentioned risks.

During FY2016, the company's overall profitability deteriorated significantly as trading gains decreased sharply from LKR 900 Mn in FY2015 to LKR 63 Mn, while the net interest income also reduced to LKR 174 Mn, compared to LKR 278 Mn in FY2015, increasing yield rates and contradictory movements of rates relative to those anticipated in view of policy measures.

PAT for the financial year was modest at LKR 11 Mn, compared to the PAT of LKR 730 Mn reported in FY 2015. ICRA Lanka notes the company's profitability performance in the current financial year (FY2017) is expected to witness some improvement, due to relatively good net interest income outlook, while the contribution from trading income is expected to be modest. The company reported a net interest income of LKR 110 Mn for the first quarter ended June 30, 2016.

### **Company Profile**

Incorporated in the year 1982, FCT is a licensed primary dealer in government securities 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 75.1% held by Dunamis Capital PLC, which is the ultimate parent of FCT.

During FY2016, FCT reported a net profit of LKR 11 Mn on a total asset base of LKR 15.3 Bn vis a vis a net profit of LKR 730 Mn on a total asset base of LKR 16.1 Bn on March 31, 2015.

In the three months ended June 30, 2016, the company reported a net profit of LKR 31 Mn on a total asset base of LKR 26.6 Bn.

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