

## ICRA Lanka assigns the issuer rating of [SL]BBB+ with stable outlook to Capital Alliance Holdings

March 28, 2019

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

### Rating action

ICRA Lanka Limited, subsidiary of ICRA Limited, a group company of Moody's Investors Service, has assigned the issuer rating of [SL]BBB+ (pronounced SL triple B plus) with stable outlook to Capital Alliance Holdings (CALH or "the Company").

### Rationale

The rating factors in CALH's status as the holding company of Capital Alliance Limited (CAL), a leading standalone primary dealer in Sri Lanka (Issuer rating of [SL]A- with negative outlook). The rating also factors in CALH's position as the holding company of the group, with entities offering various financial services, including stock brokering, asset management and corporate advisory services; contribution to net profits from these businesses however is quite modest at present. CALH's performance is therefore highly dependent on CAL. The rating takes note of CALH's moderate standalone leverage of 2.28 times (3.46 times in March 2018 and 2.42 times in March 2017) and net worth of LKR 505 Mn in December 2018 and its modest standalone earnings profile. Going forward, CALH is expected to be a non-operating holding company of the group and its current investments in debt securities of non-group entities would be realized at respective maturities. Therefore, ICRA Lanka expects CALH's gearing and liquidity likely to improve from current levels. Further, ICRA Lanka envisages support from the promoters or other promoter-owned entities (Jetwing group of companies), if required. Going forward, performance of the subsidiaries, especially CAL, and maintaining healthy levels of capitalization and liquidity, are key from a rating perspective.

### Outlook: Stable

The outlook may be revised to "Positive" if CALH's standalone financial profile improves significantly or if the risk profile of the subsidiaries, especially CAL, improves. The outlook may be revised to "Negative" in case of an increase in standalone leverage, weakening in its liquidity and earnings or in case of a deterioration in the risk profile of CAL.

### Key rating drivers

#### Credit strengths

**Holding company of CAL; other group entities offer diverse financial services:** CALH's subsidiary, CAL, is a leading primary dealer in Sri Lanka (90.4% owned by CALH). CALH is expected to continue to benefit from the dividend flow from its primary dealer operation. Other group entities offering financial and capital market services create synergies, whilst diversifying income sources. Nevertheless, contribution from these businesses is relatively modest currently. Capital Alliance Partners Limited, which provides corporate finance advisory services reported a total fee income of LKR 271 Mn in FY2018 (LKR 61 Mn in FY2017). The

asset and wealth management division, Capital Alliance Investments, reported a total income of LKR 191 Mn in FY2018 (LKR 145 in FY2017); total assets under management stood at LKR 23 Bn in December 2018. Capital Alliance Securities (Pvt) Limited, a licensed stock broker on the Colombo Stock Exchange, reported an income of LKR 137 Mn in FY2018 (LKR 101 in FY2017). Income from the IT division and from standalone investments was together LKR 58 Mn in FY2018 (LKR 7 Mn in FY2017). During FY2018, CALH divested its holdings in the tea brokering business, Ceylon Tea Brokers, to a promoter group member as it is not part of the financial services business.

## Credit challenges

**Group performance is significantly dependant on CAL:** Group performance is largely driven by the primary dealer operation, which represented over 80% of consolidated assets and 65% of group operating income in FY2018; thus, the group is susceptible to risks inherent to the primary dealer business.

**Modest standalone earnings profile:** As a holding company, CALH is primarily dependent on the dividend income flow from its key operating subsidiary, the primary dealer business. For FY2018, dividend income stood at LKR 140 Mn vis-à-vis LKR 200 Mn in FY2017, which accounted for 52% and 64% respectively of the recurring total income. The Company reported net profits of about LKR 761 Mn in FY2018 on the back of one-off capital gains of LKR 731Mn (gains from the divestment of its tea brokering subsidiary amounting to LKR 313 Mn and gains from shares repurchase of CAL amounting to LKR 418 Mn), while net profits in FY2016 and FY2017 stood at about LKR 115-120Mn per annum. ICRA Lanka expects the Company's earnings to remain under pressure in the current fiscal as CAL's earnings weakened and, expects same to remain linked to CAL's performance going forward as contribution from other subsidiaries is quite modest.

**Moderate capitalization profile presently; likely to improve:** Standalone networth of CALH stood at LKR 505 Mn as in December 2018, with gearing at 2.28 times. ICRA Lanka takes note of the dividend payouts and share re-purchases over the period FY2016-FY2018, which has kept the networth at range-bound levels during this period. As in December 2018, the Company has investments in subsidiaries and in debt and equity securities of non-group entities of about LKR 605 Mn and LKR 1,056 Mn respectively. CALH is expected to redeem its investments in debt securities of non-group entities at respective maturities, which would improve its gearing. As in December 2018, the Company has unutilized bank lines of around LKR 600 Mn. ICRA Lanka envisages support from the promoters or other promoter-owned entities (Jetwing group of companies), if required. Ability to keep gearing under control going forward would be crucial, considering the lumpy nature of cash flows of holding companies.

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

**Links to applicable criteria:** [ICRA Lanka Issuer Rating Methodology](#)

## About the Company:

Capital Alliance Holdings (CALH), through its subsidiaries provides a wide range of financial and capital market solutions. At standalone level, the Company is engaged in managing its subsidiaries i.e. Capital Alliance Limited (CAL) which is an authorized primary dealer of government securities, Capital Alliance Partners Limited, which provides advisory services on debt placements, equity raising, mergers and acquisitions and corporate restructurings, Capital Alliance Investments Limited involved in asset management and private wealth management, Capital Alliance Securities (Pvt) Limited involved in stock brokering, and Finnovation (Pvt) Limited which provides IT solutions for group entities and third parties.

For the financial year ended March 31, 2018, CALH on a stand-alone basis reported a net profit of LKR 761 Mn, on a total asset base of LKR 2.3 Bn, vis-à-vis net profit of LKR 118 Mn on a total asset base of LKR 1.9 Bn during the previous fiscal. For the 9M ended December 31, 2018, CALH reported a stand-alone net loss of LKR 12 Mn on a total asset base of LKR 1.7 Bn.

For the financial year ended March 31, 2018 CALH's consolidated net profit stood at LKR 673 Mn, on a total asset base of LKR 12.8 Bn, vis-à-vis a net profit of LKR 215 Mn on a total asset base of LKR 9.7 Bn during the previous fiscal.

## Key financial indicators (Audited)

### Stand-alone

	FY2017	FY2018	9M FY2019*
Total Income	328	282	105
Profit after Tax	118	761	(12)
Net worth	560	517	505
Total Assets	1,914	2,308	1,715
Return on Equity	22.0%	141.4%	-3.1%
Return on Assets	6.1%	36.1%	-0.8%
Reported Gearing (times)	2.42	3.46	2.28

\*Unaudited

### Consolidated

	FY2016	FY2017	FY2018
Total Income	1,203	1,441	2,534
Profit after Tax	(32)	215	673
Net worth	1,343	1,588	1,622
Total Assets	8,719	9,696	12,810
Return on Equity	-4.2%	13.0%	36.5%
Return on Assets	-0.7%	2.3%	6.0%
Reported Gearing (times)	4.86	4.36	5.82

## Rating history for last three years

Instrument	Amount Rated (LKR Mn)	Current Rating FY2018 Feb-19	Chronology of Rating History for the last 3 years		
			FY2017	FY2016	FY2015
Issuer rating	N/A	[SL]BBB+ (stable)	N/A	N/A	N/A

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