

## ICRA Lanka assigns [SL]BBB rating with Negative outlook to the proposed debenture programme of Citizens Development Business Finance PLC

October 03, 2019

Instrument*	Previous Rated Amount (LKR Mn)	Current Rated Amount (LKR Mn)	Rating Action
Subordinated, Unsecured, Listed Redeemable Debentures Programme	N/A	1,250	[SL]BBB (Negative); assigned
Issuer Rating	N/A	N/A	[SL]BBB+ (Negative); outstanding
Subordinated, Unsecured, Listed Redeemable Debentures Programme	928	928	[SL]BBB (Negative); outstanding
Trust Certificates Programme of Citizens Development Business Finance PLC Trust-03	628	628	[SL]A-(SO) (Negative); outstanding
Subordinated, Unsecured, Listed Redeemable Debentures Programme	2,000	2,000	[SL]BBB (Negative); outstanding
Subordinated Guaranteed Listed Redeemable Debentures Programme	1,000	1,000	[SL]A-(SO) (Stable); outstanding
<b>Total</b>	<b>4,556</b>	<b>5,806</b>	

### Rating action

ICRA Lanka Limited, subsidiary of ICRA Limited, a group company of Moody's Investors Services, has assigned the issue rating of [SL]BBB (pronounced S L Triple B) with Negative outlook for the proposed LKR 1,250 Mn (an initial issue of LKR 500 Mn with the option to raise a maximum of LKR 1,250 Mn) Subordinated Unsecured Redeemable Debentures Programme to be listed on the Colombo Stock Exchange.

ICRA Lanka has an issuer rating outstanding of [SL]BBB+ with Negative outlook for Citizens Development Business Finance PLC (CDB or the Company). ICRA Lanka also has outstanding ratings of [SL]BBB (pronounced SL triple B) with Negative outlook for the LKR 928 Mn and LKR 2,000 Mn Subordinated, Unsecured, Listed Redeemable Debentures Programmes.

ICRA Lanka also has an outstanding issue rating of [SL]A-(SO) (pronounced SL A minus structured obligation) with Negative outlook for the Trust Certificates Programme of Citizens Development Business Finance PLC Trust-03. The letters SO in parenthesis suffixed to a rating symbol stand for structured obligation. A 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.

ICRA Lanka has also a rating of [SL]A-(SO) (pronounced SL A minus structured obligation) with Stable outlook outstanding for the LKR 1,000 Mn Subordinated Guaranteed Listed Redeemable Debentures of the Company, guaranteed by Seylan Bank PLC (Seylan). The rating for the subordinated guaranteed redeemable debentures programme is based on the strength of the unconditional and irrevocable guarantee from Seylan Bank PLC (Seylan) covering the principal and two interest instalments (semi-annual) of the rated issue. The guarantor undertakes the obligation to pay, on demand from the trustee, the total principal sum of LKR 1,000 Mn and, two half yearly interest instalments of the proposed redeemable debentures. The

rating also assumes that the guarantee will be duly invoked by the trustee, as per the terms of the underlying trust deed and guarantee agreement, in case there is a default in payment by CDB.

## Rationale

The issue rating factors in CDB's established track record, experienced senior management team, and exposure to relatively less risky asset classes. The rating however factors in the continued weakness in CDB's capitalisation and asset quality profiles. CDB's gearing (adjusted for revaluation reserve) ratio moderated from 9.5 times as of Mar-19 to 7.9 times as of Jun-19 largely because of the capital infusion of about LKR 1 Bn in Jun-19 via a rights issue programme. The Company's Tier I and Total capital adequacy ratios (CAR) stood at 8.94% and 11.62% as of Jun-19 vis a vis the regulatory threshold of 6.50% and 10.50% respectively. The Tier I and Total CAR requirements are estimated to further moderate to about 8.73% and 11.41% post the cash dividend announced of about LKR 170 Mn. CDB's gross NPA ratio (GNPA%) increased to 8.0% as of Jun-19 vis a vis 6.6% as of Mar-19 (3.1% as of Mar-18), and delinquencies in 90+ day past due (dpd) increased to 19.7% vis a vis 15.3% (11.2% as of Mar-18), largely because of macro-economic challenges. CDB's NPAs excluding repossessed assets stood at 5.4% as of Jun-19.

ICRA Lanka further takes cognizance of the Company's sizable asset liability mismatches in the short-term because of high dependence on short-term public deposits, and decline in CDB's profitability indicators. Going forward, the Company's ability to further improve its capitalization, asset quality and earnings profile would be crucial from a rating perspective.

## Outlook: Negative

The outlook may be revised to "Stable" based on CDB's ability to improve its capitalisation and asset quality profiles while achieving healthy profitability indicators. The ratings may be downgraded in case of further weakening in the capital structure or deterioration in the asset quality indicators leading to weakening in the earnings profile from current levels.

## Key rating drivers

### Credit strengths

**Established track record and experienced senior management team:** CDB was established in 1995; it has a robust franchise and an experienced management team. The Company has about 71 outlets (including service centres) and has access to about 600+ ATM machines (in alliance with Commercial Bank) across the island as of Jun-19. CDB is one of the relatively large non-banking financial institution with an asset base of LKR 90 Bn as of Jun-19. The senior management team holds about 16% stake in the Company and are experienced professionals in the retail financing business. The management team has been associated with the Company for over a decade and there has not been any significant attrition in the senior management over the last 5-6 years.

**Exposure to relatively less risky asset classes;** About 96% of CDB's portfolio is backed by assets (vehicles/property), with 86% being as lending for vehicles. Cars and vans accounted for about 60-62% of the total portfolio since Mar-17. CDB's exposure to 3-wheelers stood at 17% as of Jun-19 vis a vis 20% as of Mar-17 (16% as of Mar-19). Cars and vans are the core asset classes of CDB, while relatively risky 3-wheelers is expected to be about 15-20% of the portfolio going forward. The Company's loan segment, which accounted for 14% of the total portfolio as of Jun-19 (11% as of Mar-19), largely comprised of property backed lending to SME and retail segments (about 4% of total portfolio), gold backed loans (4%), personal loans (3%) and loans against fixed deposits (2%). CDB envisages to achieve a portfolio mix with 75% being motor loans and 25% as non-motor loans, going forward.

## Credit challenges

**Subdued capital profile:** CDB's gearing (adjusted for revaluation reserve) at 7.9 times was relatively high when compared to peers. However, it improved from about 9.5 times each as of Mar-19 and Mar-18 because of CDB's equity capital raising of about LKR 1 Bn and moderation in borrowings during Q1FY2020 as growth was muted. CDB's Tier I and Total CAR stood at 8.94% and 11.62% as of Jul-19 vis a vis the regulatory requirement of 6.50% and 10.50% respectively. The Tier I and Total CAR requirements are estimated to further moderate to about 8.73% and 11.41% post the cash dividend announced (about LKR 170 Mn). In July 2019, Central Bank of Sri Lanka instructed CDB to adjust its investment of about LKR 1.4 Bn in Ceylinco Insurance PLC from the capital adequacy computation and granted time to deduct the same over 3-years starting from Mar-19. ICRA Lanka notes that this would continue to keep CDB's capital adequacy ratios under pressure, hence affecting the Company's ability to achieve the envisaged portfolio growth (about 20%), until commensurate capital is raised to supplement the capital base. ICRA Lanka notes the initiatives taken by the Company to raise Tier II capital in the near term. CDB's ability to secure external capital and maintain a comfortable risk-adjusted capital profile would be key monitorable going forward.

**Deteriorated asset quality:** CDB's delinquencies in 90+dpd increased to 19.7% as of Jun-19 from 15.3% as of Mar-19 and 11.2% as of Mar-18. The Company's gross NPA ratio (GNPA%) stood at 8.0% as of Jun-19 lower than the Non-Bank Financial Sector average of 9.2%. However, the same has increased from 6.7% as of Mar-19 and 3.1% as of Mar-18. The GNPA% when adjusted for repossessed stock stood at 5.4%, 4.2% and 2.4% respectively. The increased slippages were witnessed largely because of macro-economic challenges, that affected the disposal income of its borrowers. CDB's collateralized nature of lending (about 96% of portfolio asset backed as of Jun-19) provides comfort with regard to the recoverability of NPA facilities. Going forward, the Company's ability to curtail future slippages, while recovering from current NPA portfolio would be critical.

**Moderation in profitability indicators:** ICRA Lanka takes note of the moderation of CDB's RoA to 2.1% in FY2019 vis a vis 2.2% in FY2018. The same decreased to 1.2% in Q1FY2020. The moderation in profitability was largely on account of sharp increase in credit cost (2.0% in Q1FY2020 vis a vis 1.3% in FY2019 and 0.6% in FY2018), because of deterioration in the asset quality of the portfolio. In addition, the net interest margin (net interest income/average total assets) moderated to about 6.5% in Q1FY2020 vis a vis 7.1% in FY2019 (6.2% in FY2018) largely on account of moderate portfolio growth. The Company's operating expenses (operating expenses/ATA) increased to about 5.0% in FY2019 vis a vis 4.7% in FY2018, however it decreased to 4.5% in Q1FY2020, largely on account of reduced marketing and promotional expenditure. CDB's fee and non-interest income moderated during Q1FY2020 to about 1.0% (1.5% in FY2019 and FY2018 each) because of decrease in business volumes. Going forward, CDB's ability to manage credit cost, as competitive pressures are expected to limit margin expansion going forward, would be crucial for incremental profitability.

**Mismatches in the short-term maturity buckets remain, notwithstanding the reduction in deposit concentration;** CDB's ALM profile is characterized by mismatches in the < 1-year bucket of 11.6% as of Jun-19 (9.9% as of Mar-19 and 14.9% as of Mar-18) because of the near-term maturity profile of its deposits. However, the same has improved when compared to Mar-18 because of long term bank borrowings (about LKR 10.5 Bn) during FY2019 and moderate growth in the portfolio. CDB's funding profile stood at about LKR 74 Bn with 59% exposure to fixed deposits. The exposure to FDs has moderated to 59% each as of Jun-19 and Mar-19 from about 66% as of Mar-18, largely because of increase in long term bank funding (29% each as of Jun-19 and Mar-19 vis a vis 20% as of Mar-18). Further, the Company has witnessed some deposit

outflow because of the non-competitive rates offered when compared to banks. The other exposures included debentures of 5%, securitised borrowings and savings deposits of 3% each.

**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:**

Citizens Development Business Finance PLC, a registered finance company, offers leasing, hire purchase, mortgage loans, gold loans and other personal loans apart from accepting deposits (fixed and savings). The Company was established in 1995 as Ceylinco Development Bank Limited. In 2009 CDB was registered under the Finance Companies Act and re-branded as Citizens Development Business Finance PLC. It was listed on the Colombo Stock Exchange in September 2010. As of Jun-18, CDB's largest shareholder were Ceylinco Insurance PLC (with an effective holding of 40%), CDB's corporate management (about 16%) and Janashakthi group (about 12%). The Company operates 71 outlets (including service centres) and has access to over 600 ATMs (in alliance with Commercial Bank) across the island as of June 2018. The Company acquired controlling stake in Unison Capital Leasing (previously known as Laughs Capital Limited) in October 2014 and currently holds about 90% shares of the Company.

During the year ended March 31, 2019, CDB (stand-alone) reported a net profit of LKR 1,710 Mn on a total asset base of LKR 89.4 Bn as compared to net profit of LKR 1,401 Mn on a total asset base of LKR 75.5 Bn in the previous fiscal year.

For the three months ended June 30, 2019, CDB reported a net profit of LKR 275 Mn on a total asset base of LKR 89.7 Bn.

### **Guarantor Profile:**

Seylan Bank PLC (Seylan) is a commercial bank in Sri Lanka with total assets of LKR 475 Bn as of Mar-19. Seylan accounted for 4.0% of the banking industry assets, 4.5% of the sector loans and advances and 4.3% of sector deposits as of March 31, 2019. Seylan commenced operations as a licensed commercial bank in 1987. Major institutional shareholders include Lanka Orix Leasing Company PLC (effective holding of 23%), Sri Lanka Insurance Corporation (15%) and Employee Provident Fund (about 10%).

Seylan recorded a total income of LKR 15,015 Mn for the 3MCY2019 and LKR 54,872 Mn for CY2018 (LKR 49,174 Mn for CY2017). The net profits of Seylan amounted to LKR 903 Mn during 3MCY2019 and LKR 3,189 Mn for CY2018 (LKR 4,430 Mn for CY2017), which resulted in RoA (PAT as a proportion of average assets) of 0.77% and 0.73% (1.16% in CY2017) for the respective periods. Seylan had gross NPA ratios of 5.96% as of Mar-19 and 5.98% as of Dec-18 (4.42% as of Dec-17) and net NPA ratios of 4.57% and 4.40% (3.10% as of Dec-17) respectively for the said periods. Seylan had a net worth of LKR 37,329 Mn as of March 31, 2019 with tier 1 capital adequacy ratio of 9.71% and total capital adequacy ratio of 12.57%.

## Key financial indicators (Audited)

LKR Mn	FY2018	FY2019	3MFY2020*
Net Interest Income	3,454	5,226	1,418
Profit after Tax	1,401	1,710	275
Net worth	7,152	8,665	9,953
Loans and Advances	59,438	69,133	69,652
Total Assets	75,502	89,432	89,706
Return on Equity	20.9%	21.6%	11.8%
Return on Assets	2.2%	2.1%	1.2%
Gross NPA	3.1%	6.6%	8.0%
Net NPA	0.9%	3.8%	4.9%
Capital Adequacy Ratio	13.9%	11.1%	12.1%
Gearing (times)	8.9	8.7	7.5
Adjusted Gearing (times)	9.5	9.4	7.9

\*Unaudited

## Rating history for last three years: Citizens Development Business Finance PLC

Instrument	Amount Rated (LKR Mn)	Current Amount rated (LKR Mn)	Current Rating		Chronology of Rating History for the past 3 years			
			FY2020		FY2019	FY2018	FY2017	
			Sep-19	May-19	Oct-18	Nov-17	Jan-17	
Issuer rating	N/A	N/A	[SL]BBB+ (Negative)	[SL]BBB+ (Negative)	[SL]BBB+ (Negative)	[SL]BBB+ (Stable)	[SL]BBB (Stable)	
Subordinated unsecured redeemable debentures	1,250	1,250	[SL]BBB (Negative)	N/A	N/A	N/A	N/A	
Subordinated unsecured redeemable debentures	928	928	[SL]BBB (Negative)	[SL]BBB (Negative)	[SL]BBB (Negative)	N/A	N/A	
Subordinated unsecured redeemable debentures	2,000	2,000	[SL]BBB (Negative)	[SL]BBB (Negative)	[SL]BBB (Negative)	N/A	N/A	
Subordinated unsecured redeemable debentures	1,000	1,000	N/A	N/A	[SL]BBB (Negative)	[SL]BBB (Stable)	[SL]BBB- (Stable)	
Subordinated guaranteed redeemable debentures	1,000	1,000	[SL]A- (SO) (Stable)	[SL]A- (SO) (Stable)	[SL]A- (SO) (Stable)	[SL]A- (SO) (Stable)	[SL]A- (SO) (Stable)	

## Rating history for last three years: Citizens Development Business Finance PLC - Trust 03:

Instrument	Amount Rated (LKR Mn)	Current Amount Rated (LKR Mn)	Current Rating		Chronology of Rating History for the past 3 years		
			FY2020		FY2019	FY2018	FY2017
			Sep-19	May-19	Oct-18		
Trust certificates	628	628	[SL]A- (SO) (Negative); outstanding	[SL]A- (SO) (Negative); outstanding	[SL]A- (SO) (Negative)	N/A	N/A

## ANALYST CONTACTS

**Mr. Vidura Welathanthri**  
+94 11 4339907  
vidura@icralanka.com

**Mr. Dasith Fernando**  
+94 11 4339907  
dasith@icralanka.com

**Mr. A.M Karthik**  
+91 44 45964308  
a.karthik@icraindia.com

## RELATIONSHIP CONTACT

**Mr. W. Don Barnabas**  
+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](mailto:info@icralanka.com); Website: [www.icralanka.com](http://www.icralanka.com)

© Copyright, 2019 ICRA Lanka Limited. All Rights Reserved.  
Contents may be used freely with due acknowledgement to ICRA Lanka.

ICRA Lanka ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA Lanka ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA Lanka rating is a symbolic indicator of ICRA Lanka's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website [www.icralanka.com](http://www.icralanka.com) or contact ICRA Lanka's office for the latest information on ICRA Lanka ratings outstanding. All information contained herein has been obtained by ICRA Lanka from sources believed by it to be accurate and reliable, including the rated issuer. ICRA Lanka however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA Lanka in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA Lanka or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA Lanka shall not be liable for any losses incurred by users from any use of this publication or its contents.