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ICRA Lanka revises the long term ratings of Dunamis Capital PLC

ICRA Lanka Limited, subsidiary of ICRA Limited, a group company of Moody's Investors Service, has revised the issuer rating of Dunamis Capital PLC (DCP) to [SL]BBB (pronounced SL triple B) with Stable outlook from [SL]BBB+ (pronounced SL triple B plus) with Stable outlook. ICRA Lanka also revised the issue ratings of the two LKR 1 Bn Senior Unsecured Redeemable Debenture programmes each, totaling LKR 2 Bn to [SL]BBB (pronounced SL triple B) with Stable outlook from [SL]BBB+ (pronounced SL triple B plus) with Stable outlook.

The revisions in the ratings factor in the depletion in DCP's core-capital base because of the impairment losses of its subsidiary, namely Premier Synthetic Leather Manufacturers (Private) Limited (PRIMO). Consequently, the standalone market value based gearing (debt/fair value based net worth) increased to high levels of 4.68 times as in March 2017 as compared with 2.14 times as in March 2016. ICRA Lanka also takes note of increase in finance cost of the company, on account of the leverage which coupled with the impairment losses impacted its overall profitability in FY2017 (net loss on a stand-alone basis for FY2017 was LKR 627 Mn vis-à-vis the loss of LKR 44 Mn in FY2016). ICRA Lanka expects the standalone profitability to remain under pressure till the leverage is brought down to reasonable levels. The ratings continue to factor in DCP's status as the holding company of First Capital Holdings PLC (FCH; issuer rating of [SL]A- with stable outlook). FCH accounted for 89% of the total asset and 72% of the revenue of consolidated DCP. FCH's performance in turn is largely dependent on the performance of First Capital Treasuries PLC (FCT; issuer rating of [SL]A- with stable outlook), as the contribution from the other FCH subsidiaries presently is quite modest. Thus, DCP's overall performance is expected to remain susceptible to the risks inherent in FCT till the other subsidiaries (including subsidiaries of FCH) scale-up and improve their contribution to the group performance. DCP is dependent on the dividend income from FCH however access to funding lines from banks and from group entities provides some comfort from a liquidity perspective.

ICRA Lanka takes cognizance of the various initiatives being taken by the company to reduce its leverage, including sale of its holdings in some subsidiaries and, disposal of non-core real estate assets and equity investments subsequent to FY 2017. The company has fully divested its holdings in PRIMO, which has been loss making (loss of LKR 182Mn in FY2017 vis-à-vis LKR 132 Mn loss in FY2016) for the past 3 years. The company has also divested some non-core real estate assets during September 2017 as part of the restructuring process and, is also looking at divesting other real estate and equity investments in the medium term. The proceeds from the above divestments amounting to LKR 1 Bn has been used to retire some of its short term borrowings. ICRA Lanka would continue to monitor the progress on the above, as reduction in leverage, in the near term, would be crucial from a rating perspective, going forward.

As in September 2017, investments account for over 90% of total assets (87% in March 2017 and 76% in March 2016). In September 2017, Investments in subsidiaries accounted for about 55% of the stand-alone asset base of the company, while investments in real estate accounted for about 27% and the trading portfolio accounted for about 8%.

As on September 30, 2017, the standalone borrowings of DCP stood at LKR 4,285 Mn (LKR 4,707 Mn in June 2017 and LKR 4,292 Mn in March 2017), of which long term debt in the form of debentures and term loans represented 49% and 8% respectively and short term debt from banks (including overdrafts) and commercial paper accounted for 3% and 40% respectively. In addition to the above, company has access to funding lines from First Capital Holdings and about LKR 1 Bn from two commercial banks, which provide comfort from a liquidity perspective.

Total income for FY2017 was LKR 350 Mn compared to LKR 460 Mn reported in FY2016., Dividend income from equity investments (including the subsidiary FCH) accounted for about 66% of the total income for FY2017 (41% in FY2016), while the gains from sale of shares and other operating income contributed to the remaining. Increase in finance cost (total interest cost LKR 348 Mn in FY2017 vis-à-vis LKR 291 Mn in FY2016) in relation to the income impacted the profitability profile of the company in FY2017, therefore it is crucial to reduce debt levels in the near term.

On a consolidated level, the financial services segment (FCH) contributed to about 72% (51% in FY 2016) of the total income and 89% (83% in FY2016) of the assets, while the real estate development segment (Kelsey) contributed to 19% (34% in FY2016) of the total income and 5% (7% in FY2016) of the total assets of DCP in FY2017. PRIMO contributed to 7% (13% in FY2016) of the group income and 2% (2% in FY2016) of the group assets in FY2017.

Company Profile

DCP was incorporated in year 1985 as "Central Securities Limited" for investing in listed entities. The name was changed to Kshatriya Holdings Limited following the change in the ownership and management. In 2010, the name was changed to Dunamis Capital PLC. DCP is a holding company and its key subsidiaries include, First Capital Holdings PLC (DCP holds about 78% equity shares), Kelsey Developments PLC (DCP holds about 80% equity shares) and Premier Synthetic Leather Manufacturers (Private) Limited (DCP holds about 100% equity shares); PRIMO was fully divested in September 2017.

During FY2017, DCP reported a consolidated net loss of LKR 356 Mn on a total asset base of LKR 35.5 Bn as compared to net loss of LKR 415 Mn on a total asset base of LKR 25.2 Bn in the previous fiscal.

The Company reported a standalone net loss of LKR 627 Mn (extraordinary losses of LKR 439Mn) on a total asset base of LKR 5.3 Bn as compared to the net loss of LKR 44 Mn on a total asset base of LKR 5.3 Bn[1] in the previous fiscal.

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[1] During the financial year ended March 31, 2017 DCP changed its accounting policy for investment in subsidiaries from historical cost accounting to fair value accounting. Accordingly, the financial statements for FY2016 and FY2015 are restated to reflect the new accounting method.

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