

Softlogic Capital PLC: Ratings reaffirmed

February 01, 2021

Instrument	Previous Rated Amount (LKR Mn)	Current Rated Amount (LKR Mn)	Rating Action
Issuer rating	N/A	N/A	[SL]BBB+; Rating watch with developing implications; reaffirmed
Senior, unsecured, listed redeemable, debentures	1,500	1,500	[SL]BBB+; Rating watch with developing implications; reaffirmed

Rating action

ICRA Lanka Limited has reaffirmed the Issuer rating of Softlogic Capital PLC (hereafter referred to as SCAP or “the Company”) at [SL] BBB+ (pronounced as S L triple B plus). ICRA Lanka has also reaffirmed the issue rating of [SL]BBB+ (pronounced as S L triple B plus) on the senior, unsecured, listed, redeemable debenture programme of SCAP. The ratings remain on watch with developing implications.

Rationale

The ratings factor in the Company’s sizeable shareholding (about 52%) in Softlogic Life Insurance (SLI; rated [SL]A/Stable for insurance financial strength), the third largest life insurer in Sri Lanka and the synergies from being part of the diversified conglomerate, Softlogic Holdings PLC (SHL; rated [SL]BBB+/Negative). ICRA Lanka, however, notes that the large capex plans of the group entities of SHL would limit its ability to provide any sizeable financial support to SCAP over the medium term. ICRA Lanka is cognizant of SCAP’s dependence on dividend income from its subsidiaries, namely SLI and Softlogic Finance PLC (SFP; issuer rating of [SL]BB-/Rating watch with developing implications), which can expose it to the risk of experiencing cashflow/dividend volatility, going forward. The ratings factor in the immediate capital needs of SFP, which may require further support from SCAP in the event the NBFIL is unable to turnaround its performance. SCAP had raised LKR 1.0 Bn in equity via rights issue in Nov-20 which was utilized towards SFP’s rights issue which also took place at same period. The ratings note the plan to acquire Abans Finance PLC (AFP, rated BB+/Negative by Fitch) in the near term and to amalgamate same with SFP. However, ICRA Lanka estimates the standalone leverage to remain moderate (1.42x in Sep-20) post the AFP acquisition. Going forward, healthy performance of the subsidiaries, and maintaining comfortable levels of liquidity and capitalization, are key from ratings perspective.

Outlook: Rating watch with developing implications

The ratings are expected to remain on watch with developing implications until the AFP acquisition is completed, and the impact on SCAP’s subsidiary, SFP is evaluated. The outlook may be revised to “Stable” if SCAP’s standalone financial profile improves significantly or if the risk profile of the subsidiaries 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 deterioration in the risk profile of its subsidiaries.

Key rating drivers

Credit strengths

Part of the Softlogic Group; sizable shareholding in Softlogic Life Insurance PLC: SCAP represents the financial services segment of the diversified conglomerate Softlogic Holdings PLC (SHL, rated [SL] BBB+ with Negative outlook). Being part of the Softlogic group provides access to managerial and financial support from the group entities and the ability to leverage synergies between different business units of the group (e.g. Asiri Hospitals and Softlogic Life Insurance). However, ICRA Lanka takes note of the large capital expenditure and high leverage of the Softlogic group, which limits SHL's ability to support SCAP financially in the near to medium term. SCAP holds a 52% controlling stake of Softlogic Life Insurance PLC, the 3rd largest life insurance provider in Sri Lanka with a market share of 16.2% as in March 2020. SLI has been able to perform well above the industry average over the last 7 years, with the company's core net profit (excluding deferred tax) at LKR 1,095 Mn and LKR 2,173 Mn in CY2018 and CY2019, respectively. The healthy internal generation of SLI is expected to support its growth capital requirements; thus SCAP may not have to extend any support to the subsidiary in the medium term. Conversely, SLI has been able to provide regular dividends to SCAP, subject to the life insurer's own regulatory capital requirements and expansion needs (dividend payout has been on average 30% in the last 5 years).

Adequate near-term liquidity: The Company does not have any sizeable repayments in FY2021 and FY2022. SCAP has structured all its debt payments into long term bullet re-payments, as opposed to regular loan amortization, which provides some comfort from a near term liquidity perspective. Further, SCAP has not provided sizable guarantees for its group companies, except for the corporate guarantee of LKR 75 Mn extended to Softlogic Stock Brokers. The standalone interest cover reduced to 0.01x in FY2020, vis-à-vis 1.23x in FY2019 (1.68x in FY2018), as SLI did not pay a dividend during FY2020; however, the same is expected to improve in FY2021 with the expected receipt of dividends from subsidiaries.

Moderate gearing profile: The standalone gearing stood at 1.42x in Sep-20 vis-à-vis 1.29x in Mar-20 (0.50x in Mar-19), as the Company has not undertaken any new investments over the last five years. The Company had also raised LKR 1.0 Bn in equity capital via a rights issue undertaken in Nov-20. Going forward, ICRA Lanka is cognizant that SCAP may need to take on fresh borrowings to complete the proposed acquisition of AFP. ICRA Lanka envisages the standalone gearing to be in the range of 1.2x - 1.5x in Mar-21, with an additional borrowing of about LKR 1.0 Bn. Consolidated gearing (net of minority shareholders) stood at 4.91x in Sep-20 and 4.38x in Mar-20 (4.29x in Mar-19); excluding public deposits, the same stood at 1.5x and 1.2x in Sep-20 and in Mar-20, respectively.

Credit challenges

Large capital requirement of subsidiaries, mainly to support Softlogic Finance PLC (SFP): As in Sep-20, SCAP was the controlling shareholder of Softlogic Finance PLC (SFP, rated [SL] BB-/Rating watch with developing implications), with 73% ownership. Due to a provisioning gap between IFRS 9 provisioning and CBSL provisioning requirements, SFP is currently operating below regulatory capital thresholds. However, SFP was able to raise around LKR 1.9 Bn via a rights issue in Nov-20 which improved its core capital. The expected amalgamation with AFP in FY2022 (AFP's net worth stood at LKR 1.7 Bn in Sep-20), is expected to improve its capital profile further. Nonetheless, ICRA Lanka notes that further temporary funding support by SCAP may be needed if SFP is unable to return to profitability from FY2022 onwards.

Lumpy earnings profile; dependence on dividend income: As in Sep-20, investments in group entities accounted for close to 75% (78% in Mar-20) of the total standalone asset base of SCAP. Correspondingly, the dividend income from the subsidiaries (mainly SLI) has been the key source of income for SCAP (1% of

recurring standalone income in FY2020 vis-à-vis 70% in FY2019 and 36% in FY2018), with the balance income represented by fee income from providing services, including fund management. ICRA Lanka notes that the dividend payouts of SLI are subject to the regulatory and growth capital requirements of that entity, which exposes SCAP to the risk of dividend/cash flow volatility going forward.

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

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

Company Profile:

Softlogic Capital PLC (SCAP) is a holding company under the Softlogic Group, a diversified conglomerate, listed on the Colombo Stock Exchange (CSE) with interests in healthcare, retail, financial services, ICT, leisure and automotive sectors. A listed company itself, Softlogic Capital PLC has two listed subsidiaries, Softlogic Life Insurance PLC, (a licensed insurance company, with 52% holding) and Softlogic Finance PLC (a licensed finance company, with 85.07% holding). The Company also fully owns Softlogic Stock Brokers (Pvt) Ltd, a licensed stock broker of the Colombo Stock Exchange and Softlogic Asset Management (Pvt) Ltd, a Licensed Unit Trust Management company.

For FY2020, SCAP (standalone) reported a net loss of LKR 267 Mn on a gross income of LKR 191 Mn, compared with a net profit of LKR 49 Mn on a gross income of 414 Mn in the previous fiscal. For the 6M ended September 2020, SCAP reported a standalone net loss of LKR 196 Mn on a gross income of LKR 117 Mn vis-à-vis a standalone net loss of LKR 112 Mn on a gross income of LKR 70 Mn in the 6M ended September 2019.

For FY2020, the SCAP group reported a consolidated net profit of LKR 1,168 Mn on a gross income of LKR 17.8 Bn, compared to a consolidated net profit of LKR 3,201 Mn on a gross income of LKR 15.0 Bn in the previous fiscal. For the 6M ended September 2020, the SCAP group reported a consolidated net loss of LKR 814 Mn on a gross income of LKR 9.1 Bn vis-à-vis a consolidated net profit of LR 671 Mn on a gross income of LKR 8.6 Mn in the same period of the prior fiscal.



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