

Synergy Finance Limited

ICRA Nepal assigns [ICRANP] IPO Grade 5 to the proposed Equity Shares (Rights Issue) of Synergy Finance Limited

Facility/Instrument	Issue Size	Grading Action (July 2017)
Rights Share Issue	NPR 118.6022	[ICRANP] IPO Grade 5 (Assigned)

ICRA Nepal has assigned “[ICRANP] IPO Grade 5”, indicating poor fundamentals to the proposed rights issue amounting NPR 118.6022 million of Synergy Finance Limited (SYFL). ICRA Nepal assigns IPO grading on a scale of IPO Grade 1 through IPO Grade 5, with Grade 1 indicating strong fundamentals and Grade 5 indicating poor fundamentals. For the grading categories 2, 3 and 4, the sign of + (plus) appended to the grading symbols indicate their relative position within the grading categories concerned. Thus, the grading of 2+, 3+ and 4+ are one notch higher than 2, 3, and 4, respectively. SYFL is proposing to come out with 25% rights issue of 1,186,022.47 numbers of equity shares of face value NPR 100/- each, to be issued to its existing shareholders at par. The proposed issue is being made to augment the capital base and is a step towards ensuring revised (higher) paid up capital requirement set by Nepal Rastra Bank (NRB), the banking sector regulator.

The lowest IPO grade reflects SYFL’s poor financial profile caused by weak assets quality (gross NPLs¹ of ~19% on mid-April 2017 vs. ~27% on Jul-16) despite some momentum witnessed in the recoveries from NPLs and Non-banking assets (NBA) in 9MFY17. The grading also remains constrained by losses accumulated over the years leading to erosion of net worth (accumulated loss of ~NPR 220 million as of mid-April 2017). SYFL was also briefly subject to “Prompt Corrective Action-PCA” of the regulator after capital breach in Jul-14 (~9% vs. minimum requirements of 11%) on account of spike in NPLs. Although short term liquidity and capitalization profile remains comfortable so far, the company is short of minimum regulatory paid up capital of NPR 800 million to be maintained by mid-July 2017 (~NPR 474 million as of now). Even upon completion of this right issue, the company will not meet minimum capital requirements. The company is seeking acquisition options by some suitable bank and hence finding feasible acquiring counterpart within the deadline remains a major challenge for the company, which otherwise will significantly impact the operations of the company. Cost of funds for the company are higher to industry average despite fair CASA profile which also weakens the competitive positioning of the company and creates challenges in incremental growth prospects.

The credit portfolio of SYFL de-grew with compounded annual rate (CAGR) ~10% from mid-Jul-13 to mid-April-17 while the deposit base de-grew with CAGR ~7% over the same period. As for funding profile, SYFL had CASA of 47% as of mid-Apr-17 vs. industry average of ~39%; however, this remains to be reflected in cost of funds which remain higher than industry average (7.40% for SYFL vs. 6.30% for industry for 9MFY17). Credit and deposit concentration however remain moderate at ~18% and ~15% among top 20 customers. As on mid-Apr-17, SYFL’s credit portfolio stood at NPR 1,619 million on a total deposit base of NPR 1,819 million, resulting in credit to core capital and deposit (CCD) ratio of ~75%. As the credit book has grown by ~21% in 9MFY17 while deposits declined, ability to achieve adequate deposit growth to support further portfolio growth remains to be seen. Additionally, achieving business growth in the competitive banking industry with fair borrower profile will remain major challenges for the company going forward.

SYFL’s reported significantly high profitability indicators for 9MFY17 on account of recoveries from NPLs and NBAs (RoNW and RoA² of ~82% of ~12% respectively). The gross NPLs for SYFL as on mid-Apr-17 stood at 19.23% compared to 26.89% as on mid-Jul-16. Despite recovery of NPLs at this quantum, the losses sustained in the past (negative RoNW of ~70% and ~60% for FY13 and FY14 respectively) had eroded the net worth base of the company significantly which still remains to be recovered fully (~NPR 220 million accumulated losses as of mid-Apr-17 remains to be recovered). Profitability profile over medium term will be largely determined by the ability of the management to recover from existing NPLs and maintain the quality of incremental credit portfolio.

¹ Non-performing loans

² Return on Net Worth and Return on Assets



SYFL breached the minimum regulatory capital requirement in Jul-14 (CRAR of ~9% vs. minimum requirement of ~11%) after continued stress over asset quality resulting in huge loss and depleting the net worth thereby affecting the tier I capital (NPLs rose from ~2% in mid-July 2012 to ~22% in mid-July 2014). For this, the company was briefly subject to PCA by NRB in August 2015 which was lifted as company met the capital adequacy norms. Most of the NPLs resulted from lending in speculative real estate transactions signifying weak underwriting norms. Current capitalization profile of the company remains adequate vis-à-vis minimum regulatory requirement of 11% (CRAR of 16.86% in mid-April 2017). Given the proposed rights issue, incremental capitalization level of SYFL is likely to remain well above the required minimum over the medium term. However, the ability of the company to raise relatively large capital (NPR 800 million to be raised by mid-Jul-17 vs. NPR 474 million as of now) within limited time span remains to be seen.

Company Profile

Synergy Finance Limited (SYFL) is a national level Class C finance company which was formed after merger of three finance companies viz; Butwal Finance, Alpico Everest Finance and CMB Finance in December 2012. SYFL is promoted by a group of individual promoters from diverse backgrounds with maximum shareholding by one shareholder at ~8% of total capital. Share capital of the company is distributed among promoter & public in the ratio of ~51:49. The shares of the company are listed on the Nepal Stock Exchange. Mr. Binit Mani Upadhyaya is the Chief Executive Officer of the company. Its registered office is located in Butwal while the corporate office is located at Kamaladi, Kathmandu.

SYFL has presence in seven districts of Nepal through its 12 branches. SYFL has market share of ~3% in terms of deposit base as well as credit portfolio of finance companies' industry as on mid-Apr-17. SYFL reported a net profit of NPR 15 million during FY16 over an asset base of NPR 2,269 million as on mid-Jul-16 as against net profit of NPR 48 million during 2014-15 over an asset base of NPR 2,192 million as on mid-Jul-15. During 9MFY17, company has reported net profit of NPR 217 million over an asset base of NPR 2,380 million. SYFL's CRAR was 16.86% and reported gross NPL was 19.24% as on mid-Apr 2017.

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