Lalitpur Finance Limited

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

Facility/Instrument	Issue Size	Grading Action (July 2016)
Rights Share Issue	NPR 187.9453 Million	[ICRANP] IPO Grade 5 (Assigned)

ICRA Nepal has assigned an "**[ICRANP] IPO Grade 5**", indicating poor fundamentals to the proposed rights issue amounting NPR 187.9453 million of Lalitpur Finance Limited (hereinafter referred to as LFC). 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. LFC is proposing to come out with 1:1 rights issue of 1,879,453 numbers of equity shares of face value NPR 100/- each, to be issued to its existing shareholders at par. The proposed issue is to augment the capital base and partly meet the revised (higher) paid up capital requirement set by Nepal Rastra Bank (NRB), the banking sector regulator.

The grading is constrained by LFC's weak underwriting norms resulting in poor asset quality (Gross NPLs[1] of 85.1% as on mid-Apr-16[2]), weak financial profile leading to net losses during the last 6 years (except FY14), erosion of networth[3] leading to negative capital adequacy (negative CRAR[4] of 7.53%[5] as of mid-Apr-16), limited franchise (2 branches) and high geographical concentration risks (presence in two districts). ICRA Nepal also takes note of the multiple restrictions on LFL following the bank's classification as "problematic" by NRB on account of extremely weak operating and financial profile. On account of the restrictions[6], the decline in portfolio has resulted in high product and customer concentration risks (real estate loans ~34% as of mid-Apr-16 vs. regulatory cap of 25% and ~66% of credit among top 20 customers as on same date) and weak recoveries have also led to issues with liquidity management and failure in refunding depositors.

A new set of promoters are in talks with NRB to acquire 45% stake in LFC and subsequently also infuse capital through rights issue to revive the company. In addition, LFC would be required to increase the capital to NPR 800 million by FY17 (vs. NPR 188 million as of now) as required by revised regulations and would remain a challenge.

The credit portfolio of LFC de-grew at a CAGR[7] of ~21% from mid-Jul-11 to mid-Apr-16 and stood at NPR 673 million as of mid-Apr-16. As on mid-Apr-16, LFC's credit portfolio stood at NPR 673 million with total deposit base of NPR 427 million resulting in significantly high CD[8] ratio of ~155%. LFC's credit portfolio comprised mainly of Term Loans (~41%), Real Estate Loans (~34%), Personal Loans (~15%), Housing loans (~7%) and others. Also, around 66% of portfolio remains concentrated among top 20 borrowers as on same date.

LFC witnessed breach of regulatory capital requirement in FY12 on account of significant increase in NPLs also leading to company's inability to grow its portfolio. The gross NPLs for LCL as on mid-Apr-16

[1] Non-performing loans
[2] Mid-Apr-16 data are unaudited and provided by management which is marginally different from published highlights.
[3] Net worth per share of ~NPR 2 against a face value of NPR 100 on account of huge losses sustained in last five years with exception of FY14
[4] Capital to risk weightage assets ratio
[5] CRAR of -7.53% as on mid-Apr-16 are based on data provided by management which is -11.86% as per published highlights of the same date.
[6] Restrictions include refund of maturing deposits, not accept fresh deposits or expand business (including loan renewals)
[7] Compounded annual growth rate
[8] Credit to deposit ratio (adjusted for net worth)

stood at 85.05% compared to 8.35% as on mid-Jul-11. Most of the NPLs resulted from weak underwriting norms. Additionally, aggressive collateral assessment has resulted in low collateral coverage in most of the cases post decline in real estate prices and would make the recoveries difficult. Poor asset quality has led to pressure on profitability indicators, with LFC reporting losses during four out of past five years. Going forward, LFC's ability to recover from NPLs will have a bearing on future profitability and assets quality.

As for funding profile, deposits have also witnessed de-growth of ~25% from mid-Jul-11 to mid-Apr-16 with restrictions on LFC to renew maturing deposits and accept fresh deposits. Due to weak recoveries LFC is also facing liquidity issues, leading to some failed cases to refund the depositors.

LFC's profitability profile remains weak on account of high NPLs coupled with high cost of deposits resulting in lower or negative NIMs[9] (3.71% for FY15 and -1.21% for 9MFY16) over last five years. This led to LFC reporting net loss of ~NPR 26 million in FY15 and net loss of ~NPR 7 million in 9MFY16. Over last five years, LFC reported profit only in FY14 (~NPR 175 million) which was supported by write-back of provisions of ~NPR 211 million on account of marginal improvement in NPLs. The losses sustained over these years has eroded net worth base of the company (Net worth per share ~NPR 2[10] as of mid-Apr-16 compared to face value of NPR 100). LFC's earnings profile going forward will largely depend on the ability of the company to recover from existing NPLs and maintain the quality of incremental credit portfolio.

As regards capitalisation, LFC reported negative CRAR of 7.53% as of mid-Apr-2016 compared to minimum regulatory requirement of 11%. New set of promoters have proposed to acquire 45% stake in LFC and subsequently infuse further capital through rights offering. LFC would need to meet the minimum regulatory capital levels for removal of restrictions imposed by NRB. Post the proposed issue (assuming full subscription), LFC's paid-up capital would increase to ~NPR 376 million compared to NPR 800 million to be met by FY17 as required by Monetary Policy of FY15/16. LFC's ability to raise capital would also remain to be seen

Company Profile

Operating since December 1995, Lalitpur Finance Limited is a national level Class C finance company having its corporate office at Lagankhel, Lalitpur. LFC is promoted by 26 individuals engaged in various profession with maximum shareholding by one shareholder at 14% of total capital (As on mid-Apr 2016). Share capital of the company is distributed among promoter & public in the ratio of 55:45. The shares of the company are listed on the Nepal Stock Exchange. Mr. Surendra Bahadur Nhuchhe Pradhan is the Chief Executive Officer of the company. LFC has been declared as "Problematic" financial institution by NRB on 30th March 2015 imposing multiples restrictions on its business.

LFC currently has presence in two districts of Nepal through its two branches. LFC has market share of 0.57% in terms of deposit base and 0.97% in terms of credit portfolio of finance companies as on mid Apr-16. LFC reported a net loss of NPR 26 million during 2014-15 over an asset base of NPR 954 million as on mid Jul-15 as against net profit of NPR 175 million during 2013-14 over an asset base of NPR 1,432 million as on mid Jul-14. Till 9MFY16, company has reported net loss of NPR 7 million over an asset base of NPR 519 million. LFC's CRAR was negative by 7.53% and reported gross NPLs were 85.05% as on mid-Apr-2016. In terms of technology platform, LFC has implemented Microbanker which is centralized throughout its branches.

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For further details please contact:

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[9] Net Interest Margins as a % of Average Total Assets

[10] Net worth per share including calls in advance is ~Rs. 4

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