GCR RATINGS

GCR affirms Letshego Ghana's issuer ratings with a Negative outlook, reflecting mounting asset quality and capitalisation pressure. Concurrently, the Unsecured Notes were downgraded to BB+$_{(GH)}$.

Rating Action

Johannesburg, 09 July 2020 – GCR Ratings ("GCR") has affirmed Letshego Ghana Savings and Loans PLC's, (formerly known as AFB (Ghana) Plc) national scale long term issuer and short-term issuer ratings of BB+$_{(GH)}$ and B$_{(GH)}$ respectively, with a Negative Outlook. Concurrently, the national scale long term issue ratings of the senior unsecured notes under the Medium Term Notes ("MTN") programme were downgraded to BB+$_{(GH)}$ from BBB+$_{(GH)}$, with a Negative Outlook.

Rated Entity / Issue	Rating class	Rating scale	Rating	Outlook/Watch
Letshego Ghana Savings and Loans PLC	Long Term issuer	National	BB+$_{(GH)}$	Negative Outlook
	Short Term issuer	National	B$_{(GH)}$	
AFB1000	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB1100	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB1200	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB1300	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB1400	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB1500	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB1600	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB1700	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB1800	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB1900	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB2000	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB2100	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB2200	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook
AFB2300	Long Term Issue	National	BB+$_{(GH)}$	Negative Outlook

AFB2400	Long Term Issue	National	BB+(GH)	Negative Outlook
AFB2500	Long Term Issue	National	BB+(GH)	Negative Outlook

Rating Rationale

Letshego Holdings Limited ("Letshego Group") acquired AFB Ghana Plc ("AFB Ghana") in January 2017. Following the acquisition, AFB Ghana rebranded to Letshego Ghana Savings and Loans PLC in September 2019. The ratings on Letshego Ghana reflect the company's relatively weak business profile in comparison to domestic commercial banks characterised by its small size, high cost of funds (CoF) and monoline operations. The ratings are also restrained by its weak asset quality, relatively weaker capitalisation and less stable funding structure, countered by good levels of liquidity. Furthermore, the ratings benefit from parental support by Letshego Group.

The company has a relatively weak business profile in comparison to domestic commercial banks, reflecting the significantly smaller and less diverse operations (by product and business lines), which are offset by strengths within its chosen niche. Diversification efforts over the last 24 months have come short due to weakening asset quality. We expect deduction at source lending will continue to account for the bulk of operations over the medium to long term, which is considered a defendable niche due to the expertise of the group. At 31 December 2019, payroll loans contributed 60.8% towards gross loans compared to 50.4% at FY18.

Capitalisation is a negative ratings factor. We expect the GCR Capital ratio to range between 16% and 18% in the next 12 to 18 months. Balancing our expectation of: 1) the conversion of Letshego Holdings GHC22.6m subordinated debt to core capital; 2) internal capital generation ranging from 25%-30%, outpacing risk weighted asset growth of approximately 5% in the rating horizon; 3) an increase in credit losses to c.10% in 12 months moderating to c7% over the next 24 months. Furthermore, we forecast a reduction in the quantum of collection expenses payable to Jumo. Given the adverse operating conditions, reserving for stage 3 and stage 2 loans (56.4% at 31 December 2019) was deemed adequate. However, we anticipate additional pressure on capital stemming from increased provisioning in response to COVID-19 asset quality pressures.

The risk position is a negative ratings factor taking into account the deteriorating high stock of non-performing loans (NPLs), 17.8% at May 2020 (12.6% at 31 Dec. 2019) and higher than average credit losses (7.1% at 31 Dec. 2019). Failure to address or reach out to distressed exposures may result in further deterioration of the NPL ratio. Initial assessments of the potential impact of the COVID-19 pandemic indicate that the company will not be immune to the sector-wide challenges which include credit extension and slower loan repayments. Positively, there is no foreign currency lending and the company is reducing the high-risk mobile lending advances, shifting towards payroll based lending.

Funding and liquidity is a positive ratings factor, reflecting the with positive asset liability mismatch. Funding is relatively more expensive and somewhat unstable in comparison to commercial banking peers in Ghana. However, in order to lower the cost of funds, the company has a strategy to grow its customer deposit book. The stable funding ratio moderated to 64.1% at 31 Dec'19 from 71.5% at FY18. Concurrently, funding is still primarily from borrowings. Liquidity is very good, mitigating some of the structural funding weaknesses, reflecting the high liquid asset coverage of short-term wholesale funding of 2.1x at 31 December 2019 and a positive asset / liability mismatch. A high proportion of the loan book is currently short term in nature (less than three months), primarily as a result of mobile loans.

The issuer ratings benefit from parental support. Letshego Ghana is wholly owned by Letshego Holdings Limited which is headquartered and listed in Botswana, delivering finance solutions to populations across 11 Sub-Saharan markets. Though not a material asset or revenue contributor, there is evidence of support from and assimilation with the parent. We believe the Letshego Group has the capacity to support the company based on its sound financial profile and good geographic diversification.

The Senior Unsecured Notes issued by Letshego Ghana under its MTN Programme have been downgraded and equalised with the issuer rating of $BB+_{(GH)}$. This follows the publication of the Criteria for the GCR Ratings Framework, together with a refinement of GCR's Rating Scales, Symbols and Definitions. These updates outlined an approach for assigning unsecured issue ratings, as well as defining and differentiating expected loss ratings. As a result of the ensuing review of the unsecured note programme, the uplift on the unsecured notes rating was rescinded, noting that the negative pledge serving as security for the notes did not provide any preferential security interest for the programme relative to other senior unsecured creditors of the issuer.

Outlook Statement

The outlook is negative, reflecting the strain of the operating environment on the financial profile. We expect the capitalisation to range between 16% and 18%, supported by the conversion of group subordinated debt, as well as internal capital generation that is quicker than risk weighted asset growth, and rising cost of risk. We expect credit losses to increase to around 10% in 2020 and improve in 2021, as the entity shifts back to higher quality lending and the operating volatility subsides. We anticipate a moderation in the positive asset liability mismatch as asset quality improves due to the loan portfolio shift, but for liquidity to remain a ratings positive.

Rating Triggers

Failure to convert group subordinated debt into core equity may lead to downward revision of the ratings. Furthermore, we could lower the ratings if: 1) credit losses are sustained at levels above 10% in the outlook horizon; 2) the positive asset liability mismatch deteriorates (driven by a lower mobile lending book) without a commensurate improvement in asset quality; or 3) the company records internal capital generation at levels lower or in line with risk weighted asset growth. Upward ratings potential is unlikely. However, we could raise the ratings if Letshego Ghana raises and maintains a higher GCR capital ratio (above 23%) over the outlook horizon, alongside sustained improvements in asset quality and credit losses to levels below 7%.

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Related Criteria and Research

Criteria for the GCR Ratings Framework, May 2019
Criteria for Rating Financial Institutions, May 2019
GCR Ratings Scales, Symbols & Definitions, May 2019
GCR Country Risk Scores, May 2020
GCR Financial Institutions Sector Risk Score, June 2020
GCR affirms the BB+$_{(GH)}$ Long-term Ghanaian rating of AFB (Ghana) Plc under the new criteria, December 2019

Ratings History

Rated Entity / Issue	Rating class	Review	Rating scale	Rating	Outlook/Watch	Date
Letshego Ghana Savings and Loans PLC	Long Term issuer	Initial	National	$BB_{(GH)}$	Stable Outlook	May 2014
	Short Term issuer	Initial	National	$B_{(GH)}$		May 2014
	Long Term issuer	Last	National	$BB+_{(GH)}$	Stable Outlook	December 2019
	Short Term issuer	Last	National	$B_{(GH)}$		December 2019
AFB1000	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	September 2016
AFB1100	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	May 2017
AFB1200	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	May 2017
AFB1300	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	November 2017
AFB1400	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	November 2017
AFB1500	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	November 2017
AFB1600	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	June 2018
AFB1700	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	June 2018
AFB1800	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	June 2018
AFB1900	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	December 2018
AFB2000	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	December 2018

AFB2100	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	December 2018
AFB2200	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	December 2018
AFB2300	Long Term Issue	Initial	National	$BBB_{(GH)}$	Stable Outlook	December 2018
AFB2400	Long Term Issue	Initial	National	$BB+_{(GH)}$	Negative Outlook	July 2020
AFB2500	Long Term Issue	Initial	National	$BB+_{(GH)}$	Negative Outlook	July 2020
AFB1000	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB1100	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB1200	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB1300	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB1400	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB1500	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB1600	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB1700	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB1800	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB1900	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018
AFB2000	Long Term Issue	Last	National	$BBB+_{(GH)}$	Stable Outlook	December 2018

AFB2100	Long Term Issue	Last	National	BBB+$_{(GH)}$	Stable Outlook	December 2018
AFB2200	Long Term Issue	Last	National	BBB+$_{(GH)}$	Stable Outlook	December 2018
AFB2300	Long Term Issue	Last	National	BBB+$_{(GH)}$	Stable Outlook	December 2018
AFB2400	Long Term Issue	Last	National	BB+$_{(GH)}$	Negative Outlook	July 2020
AFB2500	Long Term Issue	Last	National	BB+$_{(GH)}$	Negative Outlook	July 2020

Risk Score Summary

Rating Components & Factors	Risk Scores
Operating environment	**6.00**
Country risk score	3.50
Sector risk score	2.50
Business profile	**-2.00**
Competitive position	-2.00
Management and governance	0.00
Financial profile	**-2.00**
Capital and Leverage	-0.50
Risk	-2.00
Funding and Liquidity	0.50
Comparative profile	**3.00**

Group support	3.00
Government support	0.00
Peer analysis	0.00
Total Score	**5.00**

Glossary

Debt	An obligation to repay a sum of money. More specifically, it is funds passed from a creditor to a debtor in exchange for interest and a commitment to repay the principal in full on a specified date or over a specified period.
Diversification	Spreading risk by constructing a portfolio that contains different exposures whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Exposure	Exposure is the amount of risk the holder of an asset or security is faced with as a consequence of holding the security or asset. For a company, its exposure may relate to a particular product class or customer grouping. Exposure may also arise from an overreliance on one source of funding. In insurance, it refers to an individual or company's vulnerability to various risks
Interest	Scheduled payments made to a creditor in return for the use of borrowed money. The size of the payments will be determined by the interest rate, the amount borrowed or principal and the duration of the loan.
Issuer	The party indebted or the person making repayments for its borrowings.
Leverage	With regard to corporate analysis, leverage (or gearing) refers to the extent to which a company is funded by debt.
Liquidity	The speed at which assets can be converted to cash. It can also refer to the ability of a company to service its debt obligations due to the presence of liquid assets such as cash and its equivalents. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Maturity	The length of time between the issue of a bond or other security and the date on which it becomes payable in full.
Rating Outlook	See GCR Rating Scales, Symbols and Definitions.

Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.

SALIENT POINTS OF ACCORDED RATING

GCR affirms that a.) no part of the rating process was influenced by any other business activities of the credit rating agency; b.) the ratings were based solely on the merits of the rated entity, security or financial instrument being rated; and c.) such ratings were an independent evaluation of the risks and merits of the rated entity, security or financial instrument.

The credit ratings have been disclosed to Letshego Ghana Savings and Loans PLC. The rating above was solicited by, or on behalf of, the rated entity, and therefore, GCR has been compensated for the provision of the ratings.

Letshego Ghana Savings and Loans PLC participated in the rating process via video conference management meetings, and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible.

The information received from Letshego Ghana Savings and Loans PLC and other reliable third parties to accord the credit ratings included:

- The audited financial results to 31 December 2019
- Four years of comparative audited numbers
- A breakdown of facilities available and related counterparties
- Industry comparative data
- Other related documents.