MOODY'S
INVESTORS SERVICE

CREDIT OPINION
22 October 2018

Update

Rate this Research

Contacts

Akin Majekodunmi, CFA | +44.20.7772.8614
VP-Sr Credit Officer
akin.majekodunmi@moodys.com

Constantinos Kypreos | +357.2569.3009
Senior Vice President
constantinos.kypreos@moodys.com

Jean-Francois Tremblay | +44.20.7772.5653
Associate Managing Director
jean-francois.tremblay@moodys.com

Carola Schuler | +49.69.7073.0766
MD-Banking
carola.schuler@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

Letshego Holdings Limited

Update to credit analysis

Summary

The Ba3/Not Prime issuer rating assigned to Letshego Holdings Limited (Letshego) captures the company's solid capitalisation and profitability, supported by its niche, low-cost, franchise. It also captures Letshego's growing diversification across regional countries, which makes the company more resilient to an adverse change in any one of its operating markets.

The rating balances these strengths against Letshego's (1) narrow, albeit gradually diversifying, business model, with a high reliance on payroll deductions for loan repayment collections, (2) high exposure to foreign exchange risk, (3) elevated asset quality risks, and (4) dependence on market-sensitive wholesale funding; although actions are being taken to address this weakness.

The Ba3 issuer rating assigned to Letshego reflects its stand-alone credit profile. No external support has been imputed in Letshego's rating given its limited importance to Botswana's (A2, Stable) payment system on account of its small scale, and given that it does not have any material customer deposits.

Credit strengths

» Letshego is gradually diversifying its business model across products and countries

» Solid capitalisation buffers

» Strong profitability supported by high margins

Credit challenges

» The credit profile of Letshego is sensitive to changes in regulatory and legal frameworks

» Capital is sensitive to Letshego's large foreign currency exposures

» Asset quality risks will remain elevated

» High reliance on wholesale market funding and weak liquidity metrics

Outlook

The company's ratings carry a stable outlook. The stable outlook reflects our expectation that the company's financial fundamentals will remain relatively stable over the next 12 to 18 months, despite elevated credit risks from its regional and lending expansion.

Factors that could lead to an upgrade

» An upgrade of the company's rating would depend on Letshego successfully developing broader African financial services operations, while maintaining strong profitability and capitalisation, and strengthening its liquidity profile.

Factors that could lead to a downgrade

» Negative rating pressure could be exerted on Letshego's rating if regional authorities in the company's main operating markets change the terms of, or impose restrictions on, the deduction (at source) of loan repayments from the wages of public-sector employees, leading to a sharp rise in bad debts and impairment costs. In addition, negative pressure could be exerted on the rating if (1) Letshego's expansion in other sub-Saharan markets, client segments and products, results in a material weakening of asset quality and profitability metrics; or (2) Letshego's capitalisation metrics were to materially weaken.

Key indicators

Exhibit 1
Letshego Holdings Limited

	H1 2018	2017	2016	2015	2014	2013	2012
Total Managed Assets (BWP Million)	9,815	9,017	7,932	7,540	6,412	5,024	4,320
Total Managed Assets (USD Million)	944	917	742	670	674	550	540
Pretax Preprovision profits / Average Managed Assets	14.8%	14.5%	14.8%	16.6%	18.6%	20.0%	23.3%
Net Income/ Average Managed Assets	7.9%	7.9%	7.9%	10.7%	12.7%	14.0%	17.5%
ROE (NPATBUI / Avg. Equity) [3]	19.0%	17.5%	15.5%	19.0%	19.5%	20.3%	26.2%
Tangible Common Equity / Tangible Managed Assets % [4]	38.1%	42.8%	45.3%	52.0%	60.8%	67.4%	63.7%
Problem Loans/Gross Loans	--	6.8%	6.6%	7.6%	4.5%	0.3%	0.8%
Problem Loans/(Shareholder Equity+ Loan Loss Reserve)	--	12.7%	11.5%	11.6%	6.5%	0.4%	0.9%
Net Charge-offs / Average Gross Loans & Leases	--	1.8%	2.4%	0.2%	0.9%	1.4%	1.0%

[1] NPATBUI refers to net profit (loss) after-tax before unusual items
[2] Tangible managed assets are assets including loan loss reserves, less intangible assets

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moodys.com for the most updated credit rating action information and rating history.

Profile

Letshego was incorporated in 1998, is headquartered in Gaborone, has been publicly listed on the Botswana Stock Exchange (BSE) since 2002 and is one of Botswana's largest indigenous BSE-listed companies, with a market capitalisation of 3.9 billion Pula (BWP) and an agenda focused on inclusive finance, that is aligned with supporting government initiatives. Through an 11-country presence across Southern, East and West Africa, the Group's inclusive finance agenda is focused on anticipating and solving the needs of financially under-served customers. Letshego serves a variety of financial needs to three key customer segments: Micro and Small Entrepreneurs (MSEs), public and private sector low and middle income earners and individuals in the informal market.

Detailed credit considerations

Letshego is gradually diversifying its (narrow) business model across products and countries

Letshego has a niche franchise specialising in unsecured loans to government and quasi-government employees under the payroll deduction model (around 68% of total loans). Under this model, loan repayments are taken directly from the employer prior to the distribution of monthly salaries. Letshego's business model benefits from a quick and efficient loan-approval and disbursement process and has historically led to fairly low credit costs and strong profitability.

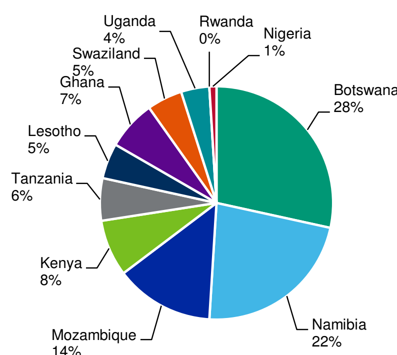
However, at the same time, its concentration to the aforementioned product exposes the company to adverse developments in the regulatory and legal framework that may either (1) hamper the payroll deduction process (although not our base case scenario)[1], and/or (2) impose or lower caps on the effective interest rate the company can charge on loans.

To counter these risks, Letshego has been increasing its geographical diversification and has a strategy to diversify its business model, by becoming a pan-African financial services company. As part of this strategy it has completed various acquisitions across Africa, has acquired banking and deposit taking licenses in several territories (it has a deposit-taking license in Ghana, Mozambique, Rwanda, Tanzania, Nigeria, and Namibia) and aims to convert its loan-only clients into transactional clients. The company currently has operations in eleven sub-Saharan African countries (Exhibit 2), with a strong niche franchise within Botswana (where it offers payroll loans to around 20% of all government employees as of June 2018), Namibia (51% of government employees), and Mozambique (22% of government employees). Outside these three markets, Letshego currently exhibits a lower franchise sustainability given its weaker brand name and lower market penetration.

Exhibit 2

Letshego's loan book is becoming increasingly diversified across countries

Loan book geographical breakdown (June 2018)



Source: Letshego

Letshego's expansion will gradually reduce its overall dependence on payroll lending (by broadening customer segments and products) and support its deposit mobilisation capabilities. However, going forward, the company will need to manage potentially elevated credit losses from (1) riskier non-payroll related loans (micro finance group loans, micro and small enterprise business loans, and low-income housing loans), albeit compensated by higher margins; (2) higher sub-Saharan Africa country risks; and (3) its relative inexperience in these newer markets and product offerings.

Asset quality risks will likely remain elevated

Letshego's business model has historically led to fairly low credit costs, reduced collection costs and improved collection statistics. As a consequence, Letshego's overall credit costs (provisions % gross loans) remained fairly low at 2.5% as at June-end 2018 (year-end 2017: 2.9%). With Letshego gradually diversifying into riskier non-payroll loans, non-performing loans (NPLs) will likely increase, although this is countered by the diversification benefits obtained. In addition, the subdued economic environment in many countries where Letshego operates, and the higher provisioning needs under new IFRS 9 guidelines (an issue faced by financial institutions globally) imply further pressure on NPLs and provisioning needs.

Letshego disclosed an NPL ratio of 7.6% as at June-end 2018, higher than the 6.8% reported in December 2017. Increasing NPLs are primarily due to (1) challenging operating conditions in some of Letshego's regional operations, such as Tanzania, Rwanda and Uganda, and (2) an increased portion of non-payroll related loans to total loans.

Reported loan loss provisions to pre-provision income were 15.5% as of June-end 2018 (19.1% for 2017), with the problem loans coverage (loan loss reserves to NPLs) improving to 95% of NPLs from 73% in December 2017. Additionally, Letshego has comprehensive credit insurance cover in markets like Namibia and Mozambique that increases the post-default recovery.

Going forward, we expect elevated asset risks to be moderated by improvements to Letshego's risk management processes. Letshego is making ongoing investments to improve automation in credit risk management.

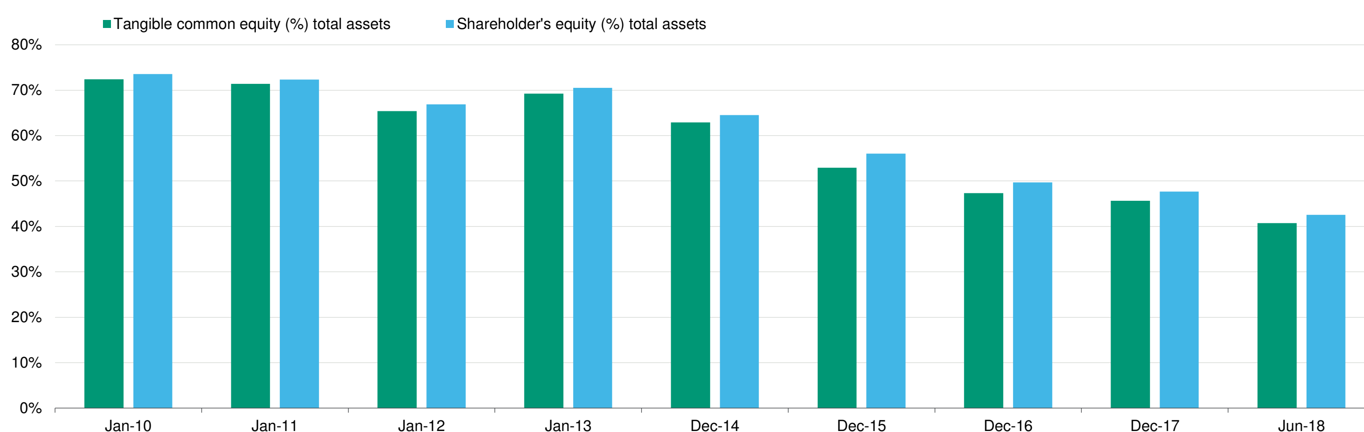
Solid capitalisation buffers, although high foreign exchange exposure poses risks

While we currently anticipate capital levels to drop further, Letshego's capitalisation level is expected to continue to underpin the current ratings. The company is currently well capitalised, with a reported shareholders' equity-to-total assets ratio of 42.6% as at June 2018 (Exhibit 3), which provides a solid buffer against any adverse changes to both the competitive environment and to its current business model.

Any material drop in capitalization, more than what we currently anticipate, could weigh on its current rating. To maximise shareholder returns, Letshego plans to increase leverage by acquiring more debt and/or reducing equity levels through share buybacks. Letshego's long-term target equity-to-total assets ratio is 30%, which still represents a robust level of capitalisation.

Exhibit 3

Letshego's capital metrics remain high, although they are on a downwards trend



Sources: Moody's Financial Metrics, Company's Financial Statements

Letshego's substantial currency risk exposure (as a result of its regional operations 72% of loans are denominated in foreign/non-pula currencies) poses a downside risk to its capital levels. An appreciation in the Botswana pula would result in a decrease of its net foreign-currency assets, leading to negative implications for tangible common equity. However, Letshego is taking steps to reduce its net foreign-currency position, although we expect the progress to be slow. Letshego also has a moderate exposure to interest-rate risk because a portion of funding is floating rate, whereas all loans are fixed rate, although the large margins allow some room for interest-rate fluctuation.

Strong profitability supported by high margins

We expect that profitability will remain sound despite declining loan yields. Loan yields have fallen on account of lower interest rates and increasing competition. While the company's diversification strategy will put some short-term pressure on profitability (through bank licensing costs and investments in fintech/information technology), this will be countered by a successful execution of its strategy that will lead to diversification benefits and will make profitability more resilient to a downturn in any one market.

The pre-provision income-to-average assets ratio remains relatively stable at 14.9% as at June-end 2018 (FY2017: 14.5%), as does the net income-to-average assets ratio at 7.9% (FY2017: 7.9%), following a 15% increase in operating income year-on-year. The cost-to-income ratio remains strong by global standards at a reported 40% as of june-end 2018, supported by Letshego's low-cost business model (the company minimises the use of inefficient branches/bricks and mortar in its operations). However, the ratio is above the company's internal target of 37%, having deteriorated from around 30% during FY2015 following (1) acquisitions in Nigeria and Tanzania (not included in 2015 figures) and (2) the company's ongoing investment spending in people, capabilities, and systems (operating expenses increased around 10% year on year, driven by increased staff, consultancy, licensing, information technology and travel costs).

It is important to note, as part of its long-term strategy, Letshego plans to derive transactional based income through customer deposit accounts, which has the potential to diversify income sources and support its profitability over time.

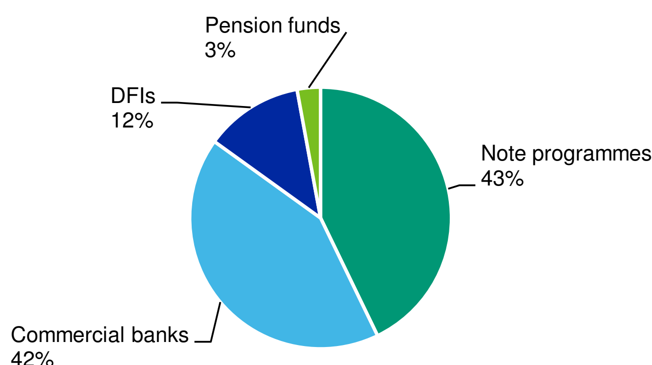
Reliance on wholesale market funding and weak liquidity metrics

While we acknowledge that a significant source of funding is in the form of equity (which is permanent and of indefinite maturity), Letshego's remaining funding is primarily wholesale, which is inherently confidence-sensitive and vulnerable to disruption. As of June 2018, bond funding accounted for 43% of total borrowings, commercial bank funding for 42%, Development Finance Institution (DFI) funding for 12% and commercial paper/pensions funds for 3% (Exhibit 4). Letshego's liquidity metrics also remain low with its 24 month coverage ratio around 23% as of June 2018 (the above ratio is calculated as the level of cash and committed, unsecured bank lines available as a percentage of debt maturing within the next 24 months).

Exhibit 4

Letshego remains wholesale funded, although increasingly more diversified

Breakdown of total borrowings (June 2018)



Source: Letshego

That said, over the past three years Letshego has diversified its funding structure, and improved its liquidity and asset and liability maturity profile through a Johannesburg Stock Exchange listed senior secured bond, senior unsecured bonds listed on the Botswana Stock Exchange (BWP300 million out of BWP2 billion had maturities of at least 10 years), and a medium term note (MTN) programme in both Ghana and Mozambique. The company plans to reduce borrowing from commercial banks and increase funding via debt capital markets, development finance institutions and customer deposits.

Source of facts and figures cited in this report

Unless noted otherwise, we have sourced data relating to system-wide trends and market shares from the central bank. Bank/Company-specific figures originate from banks' reports and Moody's Banking Financial Metrics. All figures are based on our own chart of account and may be adjusted for analytical purposes. Please refer to the document Financial Statement Adjustments in the Analysis of Financial Institutions, published on 09 August 2018.

Rating methodology

The principal methodology used in this rating was Finance Companies published in December 2016. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

Rating methodology and scorecard factors

Exhibit 5

Letshego Holdings Limited

Rating Factors	Aa/A	Baa	Ba	B	Caa	Historical View	Forward View
Non-Financial Factors						**Ba**	**Ba**
Factor: Franchise Positioning						**B**	**B**
- Market Position and Sustainability			x				
- Operational Diversification				x			
Factor: Risk Positioning						**Ba**	**Ba**
- Potential Volatility of Assets/Cashflows			x				
- Governance and Management Quality	x						
- Risk Management			x				
- Key Relationship Concentrations	x						
- Liquidity Management				x			
Factor: Operating Environment						**Ba**	**Ba**
- Economic Strength				x			
- Institutional Strength			x				
- Susceptibility to Event Risk			x				
Financial Factors						**B**	**B**
Factor: Profitability						**Aa/A**	**B**
- PPI / AMA	**15.28%**						
- Net Income / AMA	**8.85%**						
- Pre-tax Income Coefficient of Variation	**4.50%**						
Factor: Liquidity						**B**	**B**
- 24 Month Coverage Ratio					**20.49%**		
- Secured Debt / Gross Tangible Assets			**23.76%**				
Factor: Capital Adequacy						**Aa/A**	**Caa**
Capital Bucket: Traditional Finance Company							
- TCE / TMA	**42.76%**						
Factor: Asset Quality						**B**	**Aa/A**
- Problem Loans / Gross Loans					**6.98%**		
- Problem Loans / (Shareholders Equity + LLR)		**6.98%**					
Scorecard estimated stand-alone credit assessment:						**Ba3**	**B1**
Assigned Rating:						**Ba3**	

Note: Scorecard extracts figures from annual reports and latest publicly available semi-annual financial statements. .
Source: Moody's Investors Service

Ratings

Exhibit 6

Category	Moody's Rating
LETSHEGO HOLDINGS LIMITED	
Outlook	Stable
Issuer Rating	Ba3
ST Issuer Rating	NP

Source: Moody's Investors Service

Instrument class

Endnotes

1 Under a scenario where authorities cease to facilitate the payroll deduction process, Letshego will be faced with an onerous change in its operating model, a sudden and substantial rise in bad debts and impairment costs (to over 10% of gross loans) and materially higher operating expenses.

© 2018 Moody's Corporation, Moody's Investors Service, Inc., Moody's Analytics, Inc. and/or their licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

CREDIT RATINGS ISSUED BY MOODY'S INVESTORS SERVICE, INC. AND ITS RATINGS AFFILIATES ("MIS") ARE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES, AND MOODY'S PUBLICATIONS MAY INCLUDE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MOODY'S DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL, FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS AND MOODY'S OPINIONS INCLUDED IN MOODY'S PUBLICATIONS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. MOODY'S PUBLICATIONS MAY ALSO INCLUDE QUANTITATIVE MODEL-BASED ESTIMATES OF CREDIT RISK AND RELATED OPINIONS OR COMMENTARY PUBLISHED BY MOODY'S ANALYTICS, INC. CREDIT RATINGS AND MOODY'S PUBLICATIONS DO NOT CONSTITUTE OR PROVIDE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT AND DO NOT PROVIDE RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. NEITHER CREDIT RATINGS NOR MOODY'S PUBLICATIONS COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MOODY'S ISSUES ITS CREDIT RATINGS AND PUBLISHES MOODY'S PUBLICATIONS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL, WITH DUE CARE, MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.

MOODY'S CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT INTENDED FOR USE BY RETAIL INVESTORS AND IT WOULD BE RECKLESS AND INAPPROPRIATE FOR RETAIL INVESTORS TO USE MOODY'S CREDIT RATINGS OR MOODY'S PUBLICATIONS WHEN MAKING AN INVESTMENT DECISION. IF IN DOUBT YOU SHOULD CONTACT YOUR FINANCIAL OR OTHER PROFESSIONAL ADVISER. ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT.

CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT INTENDED FOR USE BY ANY PERSON AS A BENCHMARK AS THAT TERM IS DEFINED FOR REGULATORY PURPOSES AND MUST NOT BE USED IN ANY WAY THAT COULD RESULT IN THEM BEING CONSIDERED A BENCHMARK.

All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MOODY'S considers to be reliable including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the rating process or in preparing the Moody's publications.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability to any person or entity for any indirect, special, consequential, or incidental losses or damages whatsoever arising from or in connection with the information contained herein or the use of or inability to use any such information, even if MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers is advised in advance of the possibility of such losses or damages, including but not limited to: (a) any loss of present or prospective profits or (b) any loss or damage arising where the relevant financial instrument is not the subject of a particular credit rating assigned by MOODY'S.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability for any direct or compensatory losses or damages caused to any person or entity, including but not limited to by any negligence (but excluding fraud, willful misconduct or any other type of liability that, for the avoidance of doubt, by law cannot be excluded) on the part of, or any contingency within or beyond the control of, MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers, arising from or in connection with the information contained herein or the use of or inability to use any such information.

NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

Moody's Investors Service, Inc., a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by Moody's Investors Service, Inc. have, prior to assignment of any rating, agreed to pay to Moody's Investors Service, Inc. for appraisal and rating services rendered by it fees ranging from $1,500 to approximately $2,500,000. MCO and MIS also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at www.moodys.com under the heading "Investor Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

Additional terms for Australia only: Any publication into Australia of this document is pursuant to the Australian Financial Services License of MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657AFSL 336969 and/or Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail investors. It would be reckless and inappropriate for retail investors to use MOODY'S credit ratings or publications when making an investment decision. If in doubt you should contact your financial or other professional adviser.

Additional terms for Japan only: Moody's Japan K.K. ("MJKK") is a wholly-owned credit rating agency subsidiary of Moody's Group Japan G.K., which is wholly-owned by Moody's Overseas Holdings Inc., a wholly-owned subsidiary of MCO. Moody's SF Japan K.K. ("MSFJ") is a wholly-owned credit rating agency subsidiary of MJKK. MSFJ is not a Nationally Recognized Statistical Rating Organization ("NRSRO"). Therefore, credit ratings assigned by MSFJ are Non-NRSRO Credit Ratings. Non-NRSRO Credit Ratings are assigned by an entity that is not a NRSRO and, consequently, the rated obligation will not qualify for certain types of treatment under U.S. laws. MJKK and MSFJ are credit rating agencies registered with the Japan Financial Services Agency and their registration numbers are FSA Commissioner (Ratings) No. 2 and 3 respectively.

MJKK or MSFJ (as applicable) hereby disclose that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MJKK or MSFJ (as applicable) have, prior to assignment of any rating, agreed to pay to MJKK or MSFJ (as applicable) for appraisal and rating services rendered by it fees ranging from JPY200,000 to approximately JPY350,000,000.

MJKK and MSFJ also maintain policies and procedures to address Japanese regulatory requirements.

REPORT NUMBER 1145477

MOODY'S
INVESTORS SERVICE