

RAM

RATINGS

## CREDIT RATING RATIONALE

## FINANCIAL INSTITUTIONS – SRI LANKA

A wholly owned subsidiary of RAM Holdings Berhad – an affiliate of Standard &amp; Poor's

## Alliance Finance PLC – Rating Review

**Financial Institution Ratings:**

Long-term: BBB[Reaffirmed]  
Short-term: P2 [Reaffirmed]

**Rating Outlook:**  
Stable**Strengths:**

- Reputable franchise
- Adequate asset quality

**Weaknesses:**

- Heavy overheads
- Increasing dependence on secured borrowings

**Principal Activities:**

Finance company engaged in hire-purchase, finance and operating leases, personal loans, share trading and acceptance of public deposits

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**Summary**

RAM Ratings has reaffirmed Alliance Finance PLC ("Alliance" or "the Company") respective long- and short-term financial institution ratings at BBB (with a stable outlook) and P2. The ratings are supported by the Company's adequate asset quality and the resultant augmentation in its capital adequacy. On the other hand, the ratings are capped by Alliance's moderate financial performance, liquidity and funding levels.

With its 52-year track record, Alliance is one of the oldest finance companies in Sri Lanka. The Company remains vigilant about the health of its loan portfolio, which accounted for about 64% of its total assets as at 31 December 2007. Accordingly, Alliance reported a better-than-average gross non-performing-loan ("NPL") ratio of 3.31% as at the same date. Considering the industry's generally deteriorating asset quality, RAM Ratings has a positive view of Alliance's ratio. Meanwhile, the Company's provisioning level remained superior at 94.92%. Concurrently, its exposure to share trading came up to a moderate 5.58% of its total assets while exposure to inventories such as cars and furniture stayed at a benign 3.73%.

Alliance's healthy asset quality had also enabled it to reduce its provisions from LKR 18.04 million in FYE 31 March 2006 ("FY Mar 2006") to LKR 14.75 million in FY Mar 2007. As a result, the Company's pre-tax profit leapt 23.67% year-on-year ("y-o-y") to LKR 100.10 million over the same span. In terms of returns on assets ("ROA"), however, the Company's performance remained at a modest 2.79% as at end-FY Mar 2007; this is expected to moderate further due to the high interest rate environment.

Meanwhile, interest-rate risk has assumed greater importance in the present context, especially when funding lines have variable rates. Alliance's funding structure has a material 31% of total funding stemming from banking lines. As a result the Company is exposed to significant interest rate risk and this will impact on its margins and profit performance. To address the heightened interest-rate risk, the Company has established a treasury department. Although this may not have a notable impact in the short term, we note that the Company has enhanced its risk-management capabilities, as underlined by its narrowing asset-liability mismatch.

Alliance's healthier asset quality and stringent provisioning policies have enabled it to maintain its ratio on net NPLs to shareholders' funds at less than 1% as at end-December 2007. Its Tier-1 and overall risk-weighted capital-adequacy ratio stood at 7.28% and 10.77% as at the same date.

## Outlook

The stable rating outlook is based on the maintenance of Alliance’s gross NPL ratio at least 30% below the industry average. In addition, RAM Ratings expects the Company’s trading exposures vis-à-vis shares and inventories to remain at current levels i.e. below 10% of total assets. In the meantime, the Company’s financial performance should be maintained at 50% of the sector average, with deposits dominating (over 55%) its funding needs and capital adequacy within regulatory limits.

Although an upward revision of its ratings are unlikely, it can materialise should the Company’s funding structure improve materially, with public deposits taking over 85% of total funding. In addition, Alliance should preserve its asset quality and maintain an above-industry-average financial performance, over 20% consistently over 2 years. Consequent to these achievements, its capital adequacy should also ameliorate.

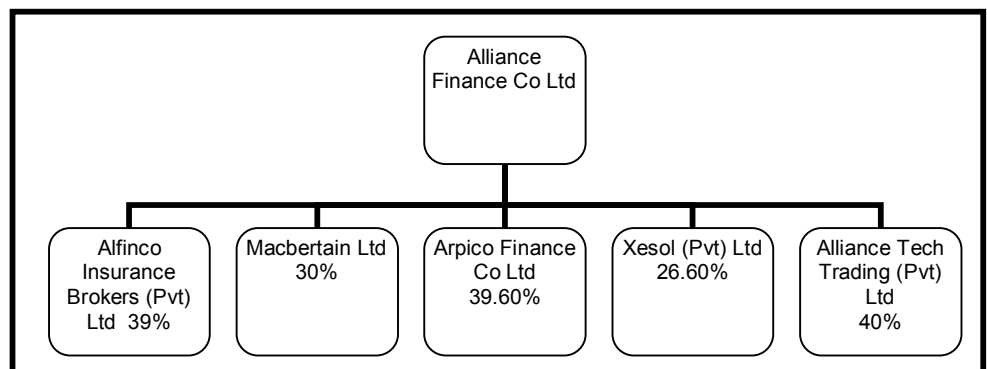
Meanwhile, there would be downward pressure on its ratings if the Company’s gross NPL ratio exceeds 80% the industry average, or its secured bank or institutional borrowings exceed public deposits. Furthermore, a downward revision can also materialise if Alliance’s financial showing deteriorates significantly i.e. less than 50% of the sector average or if there are any regulatory violations on its part. Moreover, the ratings may encounter downward pressure if its exposure to share trading exceeds current levels in relation to its total assets or capital funds.

## Corporate Profile

Alliance is the third-oldest finance company in Sri Lanka, and is regulated by the non-bank financial institutions supervision department of the Central Bank of Sri Lanka (“Central Bank”). Alliance has the distinction of being the first registered finance company (“RFC”) to obtain ISO9001:2000 certification. During its 52-year history, the Company has established itself as one of the more stable finance companies. However, its first fully fledged branch was only opened in FY Mar 2006. We note that Alliance is one of only 6 finance companies listed on the Colombo Stock Exchange (“CSE”), and is the flagship of the Alliance Group. The other companies within this group are engaged in finance, manufacturing, importing and trading activities (refer to Chart 1).

**Third-oldest  
RFC**

**Chart 1: Alliance’s corporate structure as at end-FY Mar 2007**



**Products and services offered**

As an RFC, the Company provides finance leases, hire-purchase (“HP”) facilities, operational leases, consumer credit, and collaboration finance<sup>1</sup>. The latter is a unique financial product for which its Deputy Chairman, Mr Romani De Silva, won 2 bronze awards as *Entrepreneur of the Year* in 2002. Moreover, the Company supplements its income from proprietary share trading, on top of importing and trading vehicles and furniture.

**Only RFC in Sri Lanka that is World Bank PCI**

Alliance is the only RFC in Sri Lanka to become a Participating Credit Institution (“PCI”) of the World Bank. This allows the Company access to concessional funding lines vis-a-vis expanding its micro-finance portfolio, particularly the financing of solar panels for households that do not have access to the national grid.

**Closely held listed entity****Ownership**

Despite being listed on the CSE, Alliance is a family-oriented concern; successive generations have held board positions in the Company. The founding members had been Messrs Eardley de Silva, Heyward Fernando, Fred Perera, Hayes Jayasundara and NM Appuhamy. Its top 20 shareholders controlled approximately 77.96% of the Company as at end-FY Mar 2007.

**Business strategy still largely unaltered****Management & Strategies**

The management team is led by its Joint Managing Director-cum-Deputy Chairman, Mr Romani De Silva. During the period under review, Alliance’s business strategy had remained broadly unchanged. The Company continued its 2-pronged strategy of expanding its financing business while diversifying into other arenas. Its conventional business lines include HP, finance and operating leases, import loans<sup>2</sup> and collaboration finance. Due to rising interest rates and the increasing cost of owning vehicles, however, Alliance is on the lookout for opportunities in the operating-leases segment.

**Key strategy to manage market risk**

To diversify further, Alliance imports and retails office and home furniture. Nevertheless, their bottom-line contributions are still negligible. Apart from this, the Company’s other revenue sources include share trading and importing vehicles. RAM Ratings’ concerns in respect of these businesses, which introduce market risk, are mitigated through their limited exposure.

**HP growth to slow down**

In the last 3 years, the Company has been focusing on expanding its HP segment. The HP market is primarily a domain for RFCs and specialised leasing companies, where financing is provided to those wishing to acquire registered (domestically used) vehicles. The HP market is still growing, as HP rentals are exempted from value-added tax, albeit at a more moderate pace owing to the high interest rate scenario

**Intensifying competition**

In the meantime, the entry of commercial banks into the finance-leasing segment since 2003 has intensified competition. Alliance, like many other finance companies, has had to contend with a decelerating portfolio growth as

<sup>1</sup> Under collaboration finance, Alliance provides working capital to other businesses. In return, Alliance has custody of the inventory and also manages cash for the client company. This business yields both fee and interest income.

<sup>2</sup> Financing letters of credit for vehicle importers.

***Expanding fleet of operating-lease vehicles***

RFCs' competitiveness is being undermined by the commercial banks' lower cost of funds. Nevertheless, finance and leasing companies leverage on their customer-centric services as a competitive advantage. Another competitive strategy is to augment branch network; Alliance has broadened its geographical presence by increasing its service centres and branches to 5 and 2, respectively.

The expansion of the Company's operating-lease business is on track. Alliance recently established a dedicated showroom to enhance its operating-lease business. The key issue in this market is the ability of the lessor in maintaining its assets, to ensure residual value. We note that Alliance is able to manage its fleet of operating-lease vehicles via its own vehicle-maintenance workshop. Moreover, most of Alliances' operating leases have buy-back options; in most instances, the customer acquires the vehicle by paying a residual value.

***Internal control systems to keep pace with growth***

Elsewhere, the internal-control study conducted by Messr Ernst & Young was concluded recently; the management is still in the process of evaluating the report and the relevant recommendations. As such, it is too preliminary for RAM Ratings to form any opinion on the implementation of these suggestions. Meanwhile, the Company has established a treasury department, with the aid of an external consultant; the department functions via a committee that meets fortnightly.

## **Corporate Governance**

***Closely monitored by Board***

The Board of Alliance consists of 7 directors, 4 of whom are non-executive directors ("NEDs"). The Board has expertise in both motor engineering and law. The Apex body is assisted by 4 committees: audit, risk management, remuneration and management. Monthly board meetings are held to keep tabs on the Company's key performance indicators pertaining to loan disbursements, collections, human resources and regulatory compliance. Operations risks are addressed by internal audits, which are conducted on different sections of the Company on a monthly basis and reported to the audit committee.

## **Asset Quality**

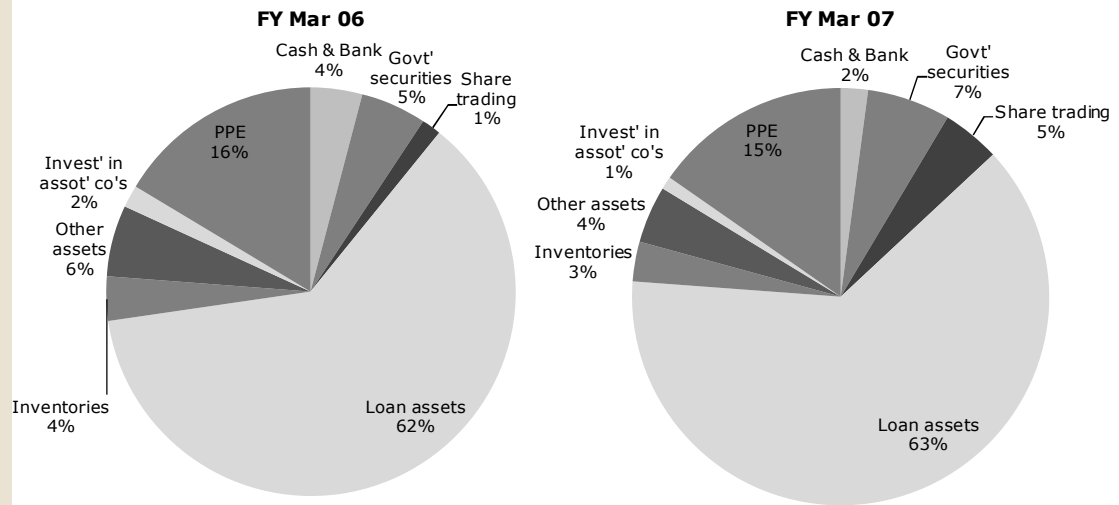
***Better-than-industry asset qualify***

Overall, RAM Ratings consider the asset quality to be better than the industry average. Even though the Company's exposure to loan assets is marginally less than industry's, it has kept its gross NPL ratio below the industry average. Apart from lending assets, RAM Ratings' opinion on Alliance's asset quality also hinges on its trading assets; the Company's current exposure to these assets is considered moderate.

***Larger exposure to share trading, but still modest***

Alliance's asset mix had been altered during the period under review. Even though loan assets still constituted a larger portion, its exposure to proprietary share trading increased between FY Mar 2006 and FY Mar 2007 (refer to Chart 2). In tandem with this, its exposure to other assets, inventories, investments in associate companies, and fixed assets contracted over the same period.

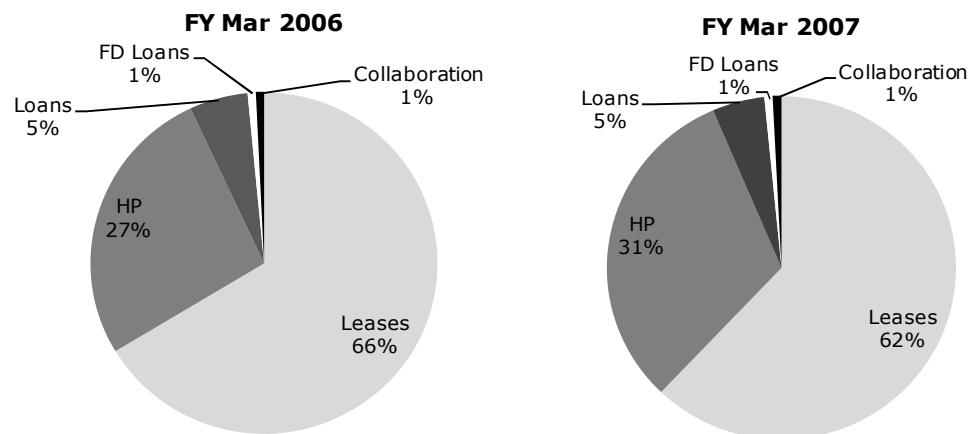
**Chart 2: Composition of Alliance’s assets as at end-FY Mar 2006 and end-FY Mar 2007**



**Vehicle financing dominates lending portfolio**

Alliance’s loan assets, which constitute about 63% of its total assets, consist of vehicle leases, HP, consumer-durable loans and loans against fixed deposits. Collaboration finance is also included in its lending assets. However, the bulk of the Company’s portfolio is taken up by leases and HP loans (refer to Chart 3) while vehicle credit accounts for about 93% (lease and HP) and other loans make up the balance; collaboration and other debtors composed a negligible 1%.

**Chart 3: Alliance’s loan composition**



**Healthy portfolio growth**

Alliance’s gross lending portfolio increased at a respectable 26.10% y-o-y in FY Mar 2007 (industry: 33.07%). Even though leases and HP had augmented by about the same absolute quantum (LKR 249.58 million and LKR 271.39 million, respectively), HP exhibited a 48.94% jump while leases only advanced 18.02% due to the base effect. Over the same period, other loans appreciated 16.61% increasing by LKR 24.16 million.

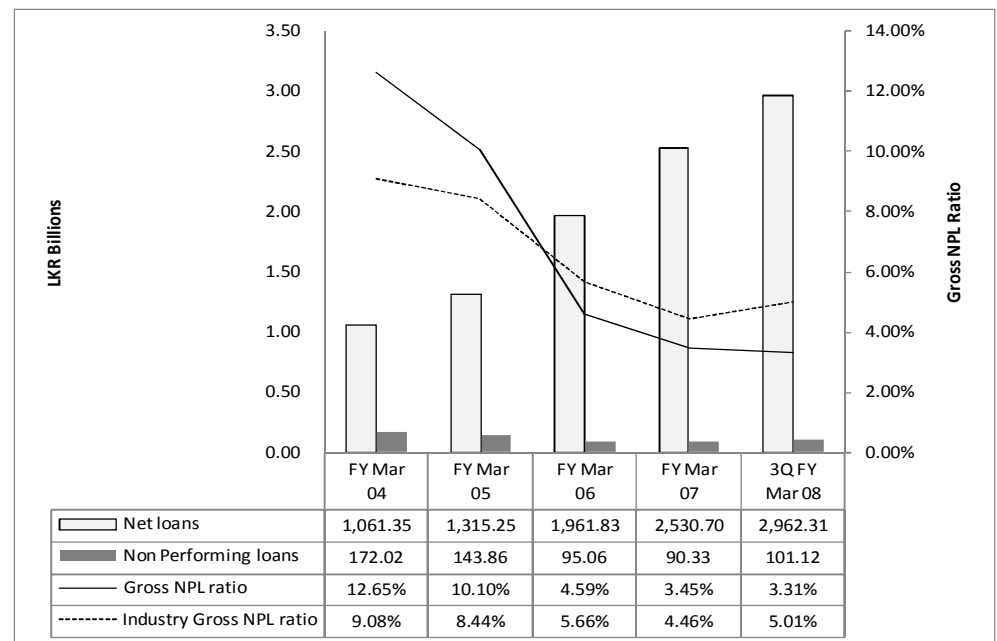
**NPL classification**

The overall quality of the Company’s lending portfolio is deemed better than industry average. Alliance classifies loans as non-performing when rentals have been in arrears for more than 6 months, as per the requirements of the Central Bank. During the year under review, its gross NPL ratio eased to 3.45% as at end-FY Mar 2007 (end-FY Mar 2006: 4.59%). This was supported by its enlarged lending portfolio and lower absolute NPLs. We note that its gross NPL ratio had ameliorated further to 3.29% as at end-December 2007.

**Stringent monitoring**

The Company trimmed its absolute NPLs by writing off loans and repossessing collateral for re-sale, which in most instances are vehicles. Thus, its level of absolute NPLs was lowered from LKR 95.06 million to LKR 90.33 million between end-FY Mar 2006 end-FY Mar 2007. Alliance’s loan portfolio is similar to those of other RFCs, i.e. mainly catering to small and medium-scale businesses that lack financial documentation. Hence, a large part of its credit evaluation depends on qualitative factors. Under these circumstances, monitoring is critical. In this respect, the Company’s improved loan monitoring is evinced by fewer new NPL classifications. Despite this, RAM Ratings notes an increase in Alliance’s absolute NPLs to LKR 101.16 as at end-December 2007 (refer to Chart 4). Given the pace of the Company’s portfolio expansion, monitoring will be vital towards maintaining its asset quality.

**Chart 4: Trends in Alliance’s asset quality vs the industry**



**Modest exposure to market risk**

Elsewhere, asset classes that introduce market risk remained below 10% of Alliance’s total assets. Exposure to trading inventories (vehicles, furniture, tiles, office equipment and ventilators) increased marginally from 3.51% as at end-FY Mar 2006 to 3.73% as at end-December 2007. Proprietary share trading, which made up 1.51% of its asset base as at end-FY Mar 2006, rose to 4.52% as at end-FY Mar 2007. RAM Ratings notes that any further increase in the Company’s equity portfolio will exert downward pressure on its ratings. In absolute terms, its exposure to share trading ascended from LKR 47.96 million to LKR 181.23 million; of the LKR 133.27 million increase, the bulk had stemmed from the finance sector.

**Firm control over operating-lease assets**

In the context of operating leases, the Company had just over 200 contracts as at end-December 2007; only 3 had been in arrears for over 6 months. Of these, Alliance had already taken possession of 2. These controls mitigate RAM Ratings’ concerns. In addition, Alliance has a vehicle-maintenance unit of its own, thus affording it the ability to maintain and manage its current fleet.

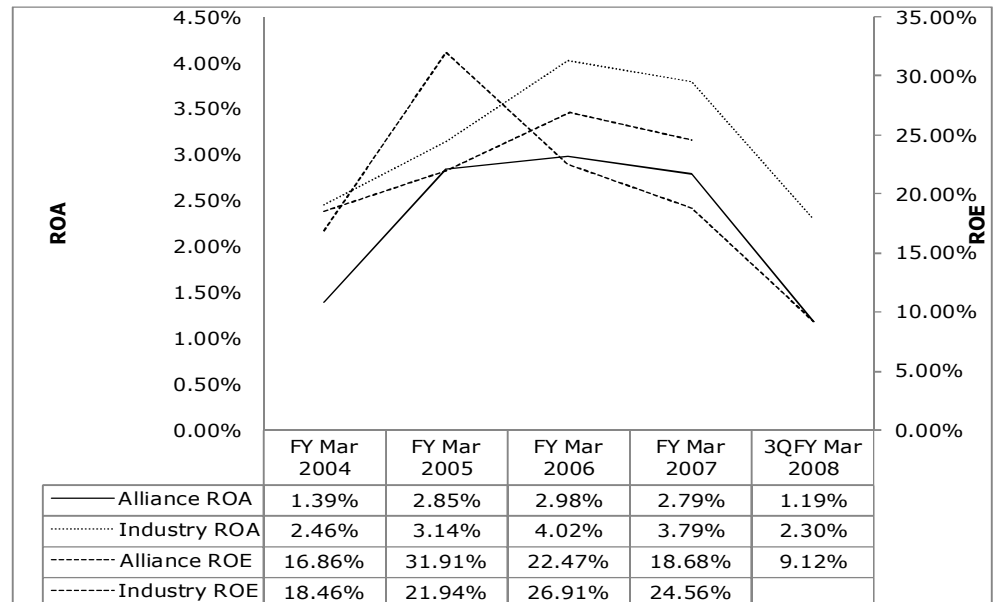
Overall, Alliance is deemed to have healthy assets. Even though we expect a rise in NPLs in the short term, its asset quality is envisaged to remain better than the sector’s average. Furthermore, asset classes that bring in market risk are expected to remain below 10% of its total assets, with exposure to share trading not increasing any further.

**Moderate financial performance**

**Performance**

RAM Ratings considers the financial performance of Alliance to be moderate; the Company’s heavier-than-industry overheads continue to subdue its performance vis-a-vis the industry. Although pre-tax profit went up 23.67% y-o-y to LKR 100.10 million in FY Mar 2007 (FY Mar 2006: LKR 80.95 million), the Company’s ROA eased to 2.79% (end-FY Mar 2006: 2.98%; FY Mar 2008: 1.72%) as its total assets had expanded 32.85% over the same span. Even though the Company’s revaluation exercise in FY Mar 2006 had influenced its performance indicators, RAM Ratings considers Alliance’s overheads as a more significant factor. For instance, the Company’s ROA, after eliminating the revaluation surplus, only inched up to 2.93% - still weaker than the industry’s 3.79%. Nevertheless, its returns on equity (“ROE”), which is influenced by gearing levels, remained better than the industry average.

**Chart 5: Profitability trends of Alliance and industry**



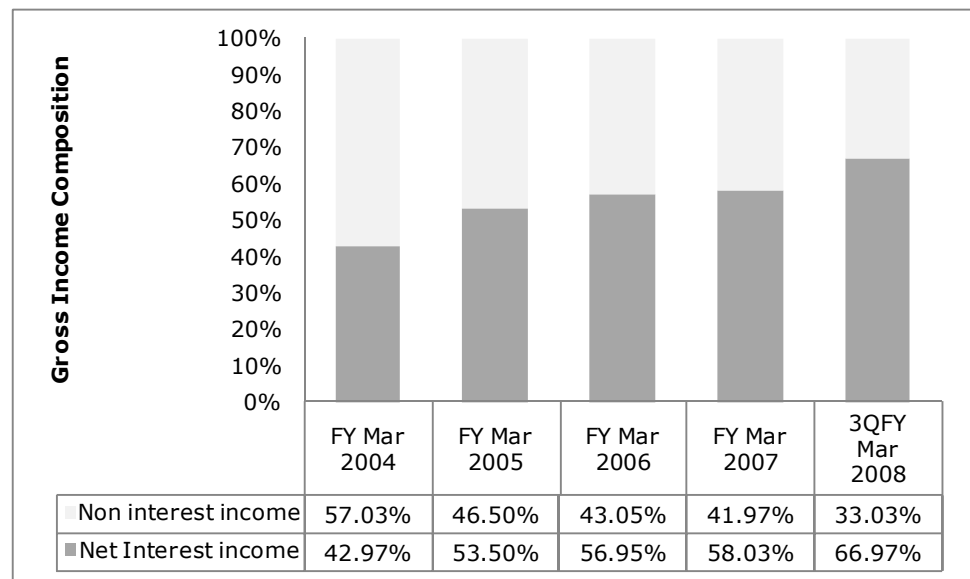
**Interest expenses rising faster**

The Company’s gross income appreciated by a modest 16.39% in FY Mar 2007, compared to the previous year’s 21.00%, as both net interest and non-interest income expansion moderated. Alliance was unable to take advantage of the 29.28% y-o-y growth in its interest income, as interest expenses had risen faster at 38.74%. With the increase in interest expenses, its interest differential contracted from 11.24% in FY Mar 2006 to 9.64% in FY Mar 2007. As a result, net interest income only increased 18.59%. Similarly, its gross-income expansion in the first 9 months to December 2007 was moderated by heightened interest expenses, which shaved its margin to 8.10%.

**Gross income mix largely unchanged**

In the meantime, Alliance’s non-interest income also advanced at a modest pace of 13.48% in FY Mar 2007, driven by profits from the sale of shares. The composition of its non-interest income receded in the first 9 months to December 2007, as trading income tapered off. As a result, non-interest income declined from 40% to 33% of the Company’s gross income mix (refer to Chart 6).

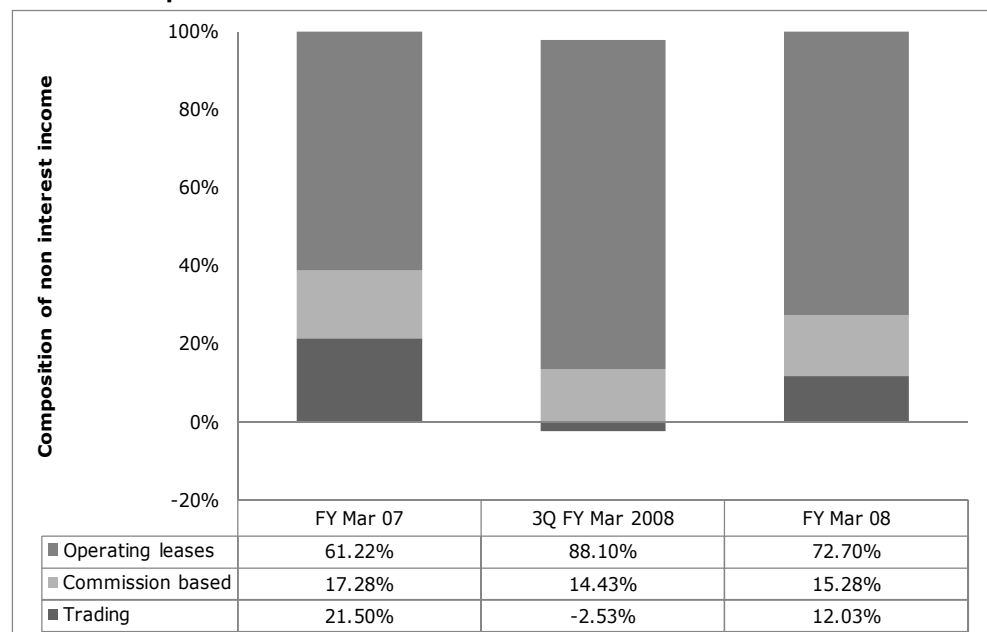
**Chart 6: Gross income composition of Alliance**



**Bulk of non-interest income from recurring sources**

Operating-lease income and service charges constitute the bulk of the Company’s non-interest income (about 80%), which is recurrent. Meanwhile, share trading and other income account for the balance. However, RAM Ratings’ concerns hinge on Alliance’s imports, which are still incurring losses. In the first 9 months to December 2007, this division’s losses eclipsed the positive contributions made by other trading activities. Consequently, the losses from trading activities had eroded the contributions from commission-based and operating-lease income (refer to Chart 7). Nonetheless, the Company was able to boost its trading income in FY Mar 2008, through collaboration finance and share trading.

**Chart 7: Composition of Alliance’s non-interest income**



**Profit performance strongly correlated to cashflow**

All said, RAM Ratings notes that even despite the losses from Alliance imports and the below industry profit performance the Company’s profits have a stronger correlation with its cashflow as its profit recognition is more prudent than that of the industry. About 35% of the industry’s gross income is non-interest; of this, some 40% is composed of real-estate income, which does not have a

**Heavy overheads**

corresponding cashflow. This is because many players recognise all their real-estate profits upon 25% to 30% payment of the sale value. On the flip side, most of Alliance’s non-interest income is directly related to cashflow. Hence, as mentioned earlier as bulk of Alliance’s non interest income is based on realised profits.

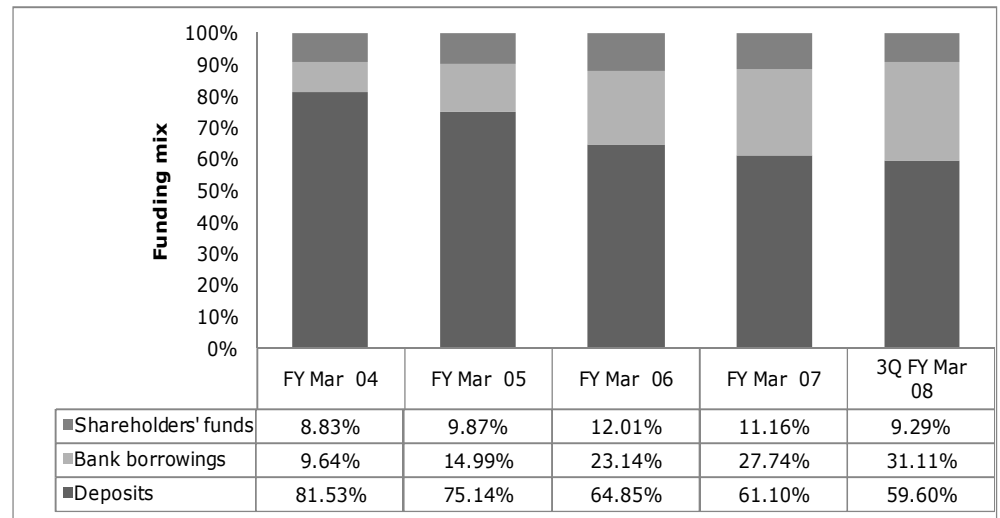
The Company’s operational efficiency, as indicated by its cost-to-income ratio of 73.63% as at end-FY Mar 2007, remains heftier than industry average of 57.85%. RAM Ratings notes that the loss incurred in the imports division, which is a service centre, is a factor that amplifies its overheads. Nonetheless, should Alliance’s profitability be materially affected by these losses it will exert a downward pressure on its ratings.

**Reduced liquidity risk**

**Funding & Liquidity**

Alliance continues to pursue a strategy of diversifying its funding base; as a result, the Company’s funding mix is significantly exposed to banking lines. Nevertheless, public deposits still take up the lion’s share of its funding composition (refer to Chart 8). The Company’s current funding strategy has improved its asset-liability profile to some extent. However, it has also heightened Alliance’s exposure to interest-rate risk. To mitigate these risks, the management has established a treasury department.

**Chart 8: Alliance’s funding mix**



**Weak funding structure**

Alliance secures bank funding by pledging its lease and HP receivables to its financiers. This strategy has assisted the Company in narrowing its funding mismatches, thus mitigating its liquidity risk (refer to Table 1). Meanwhile, its newly formed treasury department monitors and manages the increased interest-rate risks. This department is steered by the treasury committee, which meets fortnightly to review the Company’s cashflow and interest rates as well as to decide on funding strategies. The committee is currently exploring the use of interest-rate swaps to manage its heightened interest-rate risk. RAM Ratings notes that there is a dearth of such instruments in the present context. On a related note, the Company’s non interest income has a stronger correlation to its cashflow, compared to other industry players who engage in real estate.

**Exposure to interest-rate risk**

Despite the Company’s reduced liquidity risk, RAM Ratings opines that Alliance’s funding structure is weak as it is exposed to interest-rate risk.

**Table 1: Alliance's asset-liability maturity profile as at end-FY Mar 2007**

| Maturity Bucket     | Interest-Earning Assets | Interest-Bearing Liabilities | Gap             | Cumulative Gap |
|---------------------|-------------------------|------------------------------|-----------------|----------------|
| <b>LKR Millions</b> |                         |                              |                 |                |
| Less than 1 Year    | 1,405.95                | 1,518.42                     | (112.47)        | (112.47)       |
| 1 to 3 Years        | 1,283.27                | 1,250.88                     | 32.39           | (80.08)        |
| More than 3 Years   | 357.55                  | 385.08                       | (27.53)         | (107.62)       |
| <b>Total</b>        | <b>3,046.77</b>         | <b>3,154.38</b>              | <b>(107.62)</b> |                |

**Table 2: Alliance's asset-liability maturity profile as at end-FY Mar 2006**

| Maturity Bucket    | Interest-Earning Assets | Interest-Bearing Liabilities | Gap               | Cumulative Gap |
|--------------------|-------------------------|------------------------------|-------------------|----------------|
| <b>LKR Million</b> |                         |                              |                   |                |
| Less than 1 Year   | 659.94                  | 968.78                       | (308.84)          | (308.84)       |
| 1 to 3 Years       | 518.69                  | 1,070.96                     | (552.27)          | (861.11)       |
| More than 3 Years  | 218.40                  | 404.05                       | (185.65)          | (1,046.76)     |
| <b>Total</b>       | <b>1,397.03</b>         | <b>2,443.79</b>              | <b>(1,046.76)</b> |                |

## Capital Adequacy

### **Capital adequacy**

Alliance's core and overall capital-adequacy ratios remained above the minimum statutory requirements of 5% and 10%, respectively. Given its firm grip on its asset quality and prudent provisioning, the Company's ratio on net NPLs to shareholders' funds was kept at a comfortable 0.94% as at end-December 2007 (end-FY Mar 2008: 3.14%) compared to the industry average of 8.80% as at the same date.

### **Equity trading to capital funds not at critical level yet**

In relation to the Company's equity portfolio, a 30% loss of value will erode its capital funds by 13.33%. While we note that this is not critical yet, any further increase may exert pressure on its ratings.

### **Capital adequacy to be maintained via issue of sub-debt**

Going forward, the Company's capital adequacy is expected to stay within regulatory parameters. RAM Ratings expects Alliance's loan growth to decelerate owing to the macro-economic situation. In tandem with this, its internal capital generation is also expected to ease. Nonetheless, the Company's capital adequacy is anticipated to remain adequate as it intends to shore up its Tier-2 capital via a debenture issue.

## Industry Overview

Sri Lanka’s gross domestic product (“GDP”) is estimated to have expanded by 6.8% in 2007 (2006: +7.7%). Growth had slowed down for all sectors, with agriculture and services recording the most acute deceleration (refer to Table 2). All sub-segments within the services sector had lost momentum, with the hotel industry reporting the steepest drop. However, the financial services, insurance and real estate sub-sectors bucked the trend, advancing by 8.7% in 2007 (2006: +8.5%).

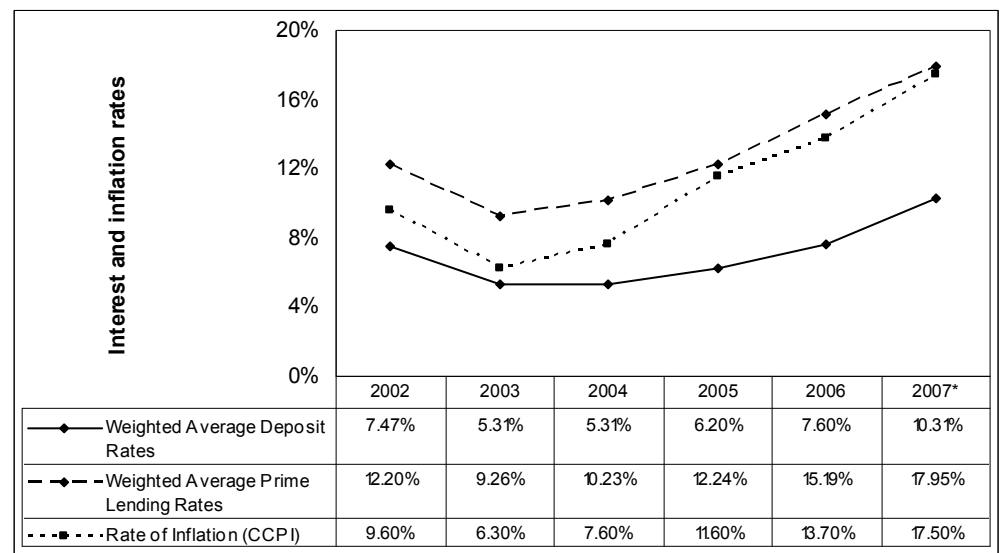
**Table 3: Overall and sectoral GDP growth**

| GDP at Constant 2002 Prices | 2006        | 2007*       |
|-----------------------------|-------------|-------------|
| Agriculture                 | 6.3%        | 3.3%        |
| Industry                    | 8.1%        | 7.6%        |
| Services                    | 7.7%        | 7.1%        |
| <b>Total</b>                | <b>7.7%</b> | <b>6.8%</b> |

\*Provisional

The domestic banking sector, meanwhile, had progressed despite rising interest rates driven by housing and consumption loans. Greater inflation is likely to have driven borrowing for consumption while easy access to credit may also have been a contributory factor. The Colombo Consumer Price Index (“CCPI”) has been trending upwards since 2003, indicating that monetary measures have not yielded the desired results. Furthermore, the steeper incline of the index since 2005 may be a reflection of the escalating hostilities in the northern and eastern parts of the country (refer to Chart 6). Against this backdrop, the weighted-average deposit rate<sup>3</sup> has been lower than the inflation rate, resulting in negative real returns for depositors.

**Chart 9: Trends in interest and inflation rates**



\*Provisional

Looking ahead, interest rates are expected to remain elevated, driven by mounting inflationary pressures - likely to continue at current levels due to escalating global commodity prices, growth in government credit and the nation’s expanding budget deficit.

<sup>3</sup> The Central Bank calculates the weighted average deposit rate monthly, based on the weighted average of all outstanding interest-bearing deposits of commercial banks and the corresponding interest rates.

Against this backdrop, the RFC industry's asset quality is likely to weaken as a whole. RFCs predominantly deal in vehicle financing, where lending rates are fixed and tenures usually extend from 36 to 48 months. Therefore, in an environment where interest rates are lofty, the borrower is locked in at a higher rate for a longer period. Meanwhile, rising inflation erodes the borrower's repayment capacity, resulting in more defaults. Given this, RFCs that cater to the sub-prime segment need to be cautious when expanding their portfolios. It is therefore vital for RFCs to become more stringent in their underwriting, and emphasise collection and recoveries.

RFCs are also likely to face heftier funding costs and a tilt in the funding structure towards the shorter end, as they are largely dependent on deposits. Commercial banks - their main competitors - enjoy lighter funding costs because of their large volumes of current and savings accounts, which bear low interest rates. In contrast, RFCs are expected to offer higher rates of interest on their deposit products. Even though the Central Bank has allowed RFCs to offer savings accounts, they are still at a disadvantage as they lack the infrastructure vis-à-vis branches and automated teller machines to effectively compete against commercial banks. To compound this, the current interest-rate environment is likely to further skew the funding structure towards the short end as depositors move their funds from long- to short-term facilities, in an effort to maximise their returns.

In addition, RAM Ratings notes RFCs' increasing tendency to pledge their portfolios with banks, in a bid to minimise mismatches between funding and lending. Even though RFCs could attain a better maturity structure from this strategy, it could also bring about concentration risk in relation to their funding structure. As these funding lines are based on floating interest rates, RFCs' capacity to manage their funding costs would be limited. While a large and diversified public deposit base reduces concentration risk, it also means greater leeway in managing funding costs.

The tendency of RFCs to chase short-term profits through trading activities, especially in real estate, is likely to expose them to a vast spectrum of risks, e.g. market, liquidity, counterparty and credit. Finance companies that are involved in housing and real-estate development tend to recognise trading profits upfront; this clouds comparison with other RFCs that offer financing products. Furthermore, trading activities also expose the RFCs' cashflows to volatility. Moreover, aggressive profit recognition could also deplete capital through excessive dividend payouts. Market risk arises due to inflated property prices, location risk, infrastructure facilities and extraneous social factors. On the other hand, counterparty risk would materialise should contractors fail to meet their obligations.

In terms of capitalisation, the RFC industry is anticipated to expand its capital base due to regulatory requirements. The Central Bank issued a directive in 2006, under which RFCs are required to have a minimum core capital of LKR 100 million by February 2007, and LKR 200 million by July 2008.

On the whole, the industry's profit performance - which is affected by all the abovementioned issues - is likely to be adversely affected. Nonetheless, RFCs with thin margins and high overheads are expected to feel the pinch much more than those with leaner structures and broader margins. Finally, resource allocation is also likely to be influenced by credit ratings as the public becomes more aware of such ratings and divert their funds towards better-managed RFCs.

## Relevant Central Bank Directions Applicable to Registered Finance Companies

|                                                   |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
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| <p><b>Liquid assets</b></p>                       | <p>Every finance company must have a minimum holding of liquid assets at any given time. Liquid assets mean:</p> <ol style="list-style-type: none"> <li>a) Cash in hand.</li> <li>b) Balances in a current or deposit account in a commercial bank, free from any banker's lien or charge.</li> <li>c) Sri Lankan Government Treasury Bills, free from any charge or lien.</li> <li>d) Sri Lankan Government Securities maturing within 1 year and free from any charge or lien.</li> <li>e) Central Bank securities maturing within 1 year and free from any charge or lien.</li> <li>f) Cash balance, if any, maintained with the Central Bank.</li> </ol> <p>The minimum limits are as follows:</p> <ol style="list-style-type: none"> <li>1. For time deposits, 15% of outstanding deposits.</li> <li>2. For certificates of deposits, 15% of the face value of the certificates.</li> <li>3. For savings deposits, 20% of the outstanding deposits.</li> </ol> <p>The companies should maintain the liquid assets in the form of (c), (d) and (e) above, equivalent to 10% of its average month-end deposit liabilities of the preceding financial year.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| <p><b>Provision of bad and doubtful debts</b></p> | <p>Every finance company had been required to follow either one of the following directions on provisioning for bad and doubtful debts until 1 April 2007:</p> <p><u>Direction No. 1 of 1991</u></p> <p>Bad and doubtful debts provided for under this direction are subject to a minimum of:</p> <ol style="list-style-type: none"> <li>(a) 50% of all advances in arrears for a period of 7 to 12 months.</li> <li>(b) 100% of all advances in arrears for 13 months or more.</li> </ol> <p>A company may deduct the value of land and buildings held as collateral for a particular advance, in arriving at the provision figure under both (a) and (b) above, subject to the following conditions:</p> <ol style="list-style-type: none"> <li>1. The value so deducted should not exceed the value decided by a professional valuer at the time of granting the advance.</li> <li>2. In the case of residential properties occupied by the borrower or a tenant, there should be an agreement to grant vacant possession in the event of the sale of such property.</li> </ol> <p><u>Direction No. 2 of 1991</u></p> <p>Bad and doubtful debts provided for under this direction are subject to a minimum of:</p> <ol style="list-style-type: none"> <li>(a) 50% of all advances in arrears for a period of 12 to 24 months.</li> <li>(b) 100% of all advances in arrears for more than 24 months.</li> </ol> <p>A new directive came into effect on 1 April 2007 (Direction No. 3 of 2006); this is very similar to Direction 1. However, Direction 3 requires all finance companies to follow a more stringent formula in the calculation of collateral value that is deductible for provisioning purposes.</p> |

|                                     |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |
|-------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                     | <p>With effect from 1 April 2007, Direction No. 3 of 2006 will be applicable to every RFC and will replace Directions 1 and 2.</p> <p><u>Direction No. 3 of 2006</u></p> <p>Bad and doubtful debts provided for under this direction are subject to a minimum of:</p> <p>(a) 50% of all advances in arrears for a period of 6 to 12 months.<br/> (b) 100% of all advances in arrears for 13 months or more.</p> <p>A finance company may deduct the value of the following items held as collateral in arriving at the amount of provisioning;</p> <ol style="list-style-type: none"> <li>1. Sri Lankan Government securities, free from any lien or charge.</li> <li>2. Central Bank securities, free from any lien or charge.</li> <li>3. Time deposits in a licensed commercial bank, specialised bank or RFC, free from any lien or charge.</li> <li>4. Bank guarantees.</li> <li>5. With regard to repossessed vehicles and machinery, 80% of the valuation obtained in the preceding 6 months and by an approved valuer.</li> <li>6. With regard to mortgaged land and buildings that are held as collateral, if the accommodation has been in arrears for a period of: <ol style="list-style-type: none"> <li>a) 6-36 months, 100% of the value is deductible</li> <li>b) 37-60 months, 80% of the value is deductible</li> <li>c) 61-120 months, 50% of the value is deductible</li> <li>d) more than 120 months, 0% of the value is deductible</li> </ol> </li> </ol> |
| <p><b>Capital adequacy</b></p>      | <p>Every finance company must maintain a minimum total risk-weighted capital-adequacy ratio of 10% in relation to its risk-weighted assets. The constituents of the capital are divided into:</p> <p>(a) Tier I - Core Capital</p> <p>This represents permanent shareholders' equity and reserves created or increased by appropriation of retained earnings or other surpluses, including share premiums, retained profits and other reserves. The core-capital ratio should constitute not less than 50%, i.e. this has to be at least half, of the total risk-weighted capital-adequacy ratio.</p> <p>(b) Tier II - Supplementary Capital</p> <p>Represents revaluation reserves, general provisions and other capital instruments which combine certain characteristics of equity and debt, such as hybrid capital instruments and unsecured subordinated debts. Supplementary capital should not exceed 100% of the core capital.</p> <p>The Central Bank also issues guidelines from time to time, to be used in computing total risk-weighted assets.</p>                                                                                                                                                                                                                                                                                                                                                                                                               |
| <p><b>Single-borrower limit</b></p> | <p>In the case of an individual borrower, the maximum of a single advance or the aggregate of advances granted to, and the aggregate outstanding at any time on advances granted to, should not exceed 10% of the capital funds of the finance company.</p> <p>This limit stands at 15% for any group of corporate or unincorporated borrowers with common directors or common partners or common proprietors.</p> <p>Capital funds generally mean paid-up capital and permanent free reserves, and may include unsecured debentures and other loan stocks if approved by the Monetary Board.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |

|                                                |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |
|------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><b>Minimum core-capital requirement</b></p> | <p>Every finance company must at all times maintain an unimpaired core capital of LKR 200 million. However, companies that could not meet this requirement by February 2006 had been granted a 30-month extension, subject to the following:</p> <ul style="list-style-type: none"> <li>(a) A finance company with a core capital of less than LKR 100 million must: <ul style="list-style-type: none"> <li>1. enhance its core capital to at least LKR 100 million by February 2007; and</li> <li>2. bring the remaining LKR 100 million or the deficit up to the core-capital requirement of LKR 200 million by July 2008.</li> </ul> </li> <li>(b) A finance company with a core capital of between LKR 100 million and LKR 200 million must bring in: <ul style="list-style-type: none"> <li>1. at least 50% of the deficient amount to meet the core-capital requirement of LKR 200 million by February 2007; and</li> <li>2. the balance of the deficient amount up to the core capital requirement of LKR 200 million by July 2008.</li> </ul> </li> </ul> |
| <p><b>Investments</b></p>                      | <p>A finance company must not invest in the shares of any company</p> <ul style="list-style-type: none"> <li>(a) In excess of 5% of its capital funds, provided that such investment does not exceed 40% of the issued share capital of the investee company</li> <li>(b) In aggregate, in excess of 25% of the capital funds of the finance company</li> </ul> <p>Capital funds generally mean paid-up capital and permanent free reserves, and may include unsecured debentures and other loan stocks if approved by the Monetary Board.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |

## Corporate Information

|                                           |                                      |                               |                                                          |                                |
|-------------------------------------------|--------------------------------------|-------------------------------|----------------------------------------------------------|--------------------------------|
| <b>Date of Incorporation:</b>             | 18 July 1956                         |                               |                                                          |                                |
| <b>Commencement of Business:</b>          | 1956                                 |                               |                                                          |                                |
| <b>Major Shareholders:</b>                |                                      |                               |                                                          |                                |
|                                           | Mr RKEP de Silva                     | 18.21%                        |                                                          |                                |
|                                           | Motor Services Station Ltd           | 12.15%                        |                                                          |                                |
|                                           | Ms DMEP Perera                       | 10.62%                        |                                                          |                                |
|                                           | Mr JEPA de Silva                     | 6.24%                         |                                                          |                                |
|                                           | Mr DFWSK Perera                      | 4.10%                         |                                                          |                                |
|                                           | Orient Hotels Ltd                    | 4.03%                         |                                                          |                                |
| <b>Directors:</b>                         |                                      |                               |                                                          |                                |
|                                           | Mr Pratapkumar de Silva              |                               | Chairman & Joint Managing Director                       |                                |
|                                           | Mr R Romani de Silva                 |                               | Deputy Chairman & Joint Managing Director                |                                |
|                                           | Mr DLSR Perera                       |                               | Director Finance Director                                |                                |
|                                           | Mr JFR De Saram                      |                               | Director                                                 |                                |
|                                           | Mr RM Canekeratne                    |                               | Director                                                 |                                |
|                                           | Mr B Ponnambalam                     |                               | Director                                                 |                                |
|                                           | Mrs KSK de Silva                     |                               | Director                                                 |                                |
| <b>Auditor:</b>                           | M/s HLB Edirisinghe & Co             |                               |                                                          |                                |
| <b>Listing:</b>                           | Listed on the Colombo Stock Exchange |                               |                                                          |                                |
| <b>Key Management:</b>                    |                                      |                               |                                                          |                                |
|                                           | Mr Romani de Silva                   |                               | Deputy Chairman/Joint Managing Director/Finance Director |                                |
|                                           | Mr Rohan Perera                      |                               | Executive Director                                       |                                |
|                                           | Mr J F R de Saram                    |                               | General Manager/Operations                               |                                |
|                                           | Mr Viville Perera                    |                               |                                                          |                                |
| <b>Major Subsidiaries and Associates:</b> |                                      |                               |                                                          |                                |
|                                           | Arpico Finance Co Ltd                | 39.59%                        |                                                          |                                |
|                                           | Alfinco Insurance Brokers (Pvt) Ltd  | 39.00%                        |                                                          |                                |
|                                           | Xesol (Pvt) Ltd                      | 26.60%                        |                                                          |                                |
|                                           | Macbertan Ltd                        | 30.00%                        |                                                          |                                |
|                                           | Alliance Tech Trading (Pvt) Ltd      | 40.00%                        |                                                          |                                |
| <b>Capital History:</b>                   | Year                                 | Remarks                       | Amount (LKR million)                                     | Cumulative Total (LKR million) |
|                                           | 1956                                 | Issue of ordinary shares      | 0.15                                                     | 0.15                           |
|                                           | 1957                                 | Issue of ordinary shares      | 0.03                                                     | 0.18                           |
|                                           |                                      | Issue of preference shares    | 0.10                                                     | 0.28                           |
|                                           | 1959                                 | Issue of preference shares    | 0.06                                                     | 0.35                           |
|                                           | 1966                                 | Redemption of ordinary shares | (0.05)                                                   | 0.30                           |
|                                           | 1967                                 | Redemption of ordinary shares | (0.05)                                                   | 0.25                           |
|                                           | 1968                                 | Issue of ordinary shares      | 0.10                                                     | 0.35                           |
|                                           | 1969                                 | Issue of ordinary shares      | 0.10                                                     | 0.45                           |
|                                           | 1970                                 | Issue of ordinary shares      | 0.90                                                     | 1.35                           |
|                                           | 1990                                 | Issue of ordinary shares      | 4.05                                                     | 5.4                            |
|                                           | 1994                                 | Issue of ordinary shares      | 10.80                                                    | 16.2                           |

## Financial Summary - Company

|                                                    | Unaudited        |                  |                  |                  |                  |
|----------------------------------------------------|------------------|------------------|------------------|------------------|------------------|
| <b>BALANCE SHEET (LKR Million)</b>                 | <b>31-Mar-04</b> | <b>31-Mar-05</b> | <b>31-Mar-06</b> | <b>31-Mar-07</b> | <b>31-Dec-07</b> |
| <b>ASSETS</b>                                      |                  |                  |                  |                  |                  |
| Cash & Money At Call                               | 93.84            | 51.20            | 17.37            | 38.89            | 51.03            |
| Deposits & Placements With Financial Ins           | 90.91            | 96.72            | 102.67           | 45.67            | 1.52             |
| Securities Purchased Under Resale Agree            | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Securities                                         |                  |                  |                  |                  |                  |
| Dealing Securities                                 | 238.32           | 266.34           | 213.64           | 439.22           | 575.34           |
| Investment Securities                              | 45.01            | 19.00            | 36.85            | 12.78            | 0.00             |
| Gross Loans & Advances                             | 1,207.41         | 1,440.90         | 2,085.91         | 2,630.43         | 3,070.84         |
| Interest-In-Suspense                               | 22.14            | 16.56            | 15.00            | 11.74            | 12.55            |
| General Loan Loss Reserves                         | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Specific Loan Loss Reserves                        | 123.93           | 109.09           | 109.09           | 87.99            | 95.99            |
| Net Loans & Advances                               | 1,061.35         | 1,315.25         | 1,961.83         | 2,530.70         | 2,962.31         |
| Investments in Subsidiaries/Associates             | 24.51            | 38.95            | 27.84            | 27.84            | 37.82            |
| Investment Land and Properties                     | 3.04             | 3.04             | 3.04             | 2.95             | 2.95             |
| Other Assets                                       | 137.95           | 179.13           | 287.68           | 298.31           | 351.12           |
| Property, Plant and Equipment                      | 277.95           | 294.09           | 519.66           | 612.96           | 649.27           |
| <b>TOTAL ASSETS</b>                                | <b>1,972.87</b>  | <b>2,263.71</b>  | <b>3,170.58</b>  | <b>4,009.32</b>  | <b>4,631.37</b>  |
| <b>LIABILITIES</b>                                 |                  |                  |                  |                  |                  |
| Customer Deposits                                  |                  |                  |                  |                  |                  |
| Savings                                            | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Fixed                                              | 1,510.31         | 1,631.10         | 1,783.89         | 2,134.45         | 2,385.11         |
| NIDs                                               | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Interbank Deposits                                 | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Bills & Acceptances Payable                        | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Securities Sold Under Repurchase Agree             | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Other Borrowing                                    | 178.61           | 325.42           | 636.66           | 969.06           | 1,245.13         |
| Subordinated Debt & Hybrid Capital                 | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Other Liabilities                                  | 120.31           | 92.97            | 243.87           | 340.23           | 453.41           |
| <b>TOTAL LIABILITIES</b>                           | <b>1,809.23</b>  | <b>2,049.49</b>  | <b>2,664.42</b>  | <b>3,443.74</b>  | <b>4,083.65</b>  |
| Paid-up Capital                                    | 16.20            | 16.20            | 16.20            | 16.20            | 16.20            |
| Minority Interest                                  | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Share Premium & Other Reserves                     | 137.22           | 181.87           | 304.40           | 327.65           | 327.90           |
| Statutory General Reserve                          | 5.10             | 11.00            | 177.07           | 213.25           | 162.10           |
| Retained Profits/(Loss)                            | 5.12             | 5.14             | 8.49             | 8.48             | 41.52            |
| <b>Total Shareholders' Funds</b>                   | <b>163.64</b>    | <b>214.21</b>    | <b>506.16</b>    | <b>565.59</b>    | <b>547.72</b>    |
| <b>TOTAL LIABILITIES &amp; SHAREHOLDERS' FUNDS</b> | <b>1,972.87</b>  | <b>2,263.70</b>  | <b>3,170.58</b>  | <b>4,009.32</b>  | <b>4,631.37</b>  |
| <b>COMMITMENTS &amp; CONTINGENCIES</b>             | <b>0.00</b>      | <b>0.00</b>      | <b>0.00</b>      | <b>0.00</b>      | <b>0.00</b>      |
| <b>TIER 1 CAPITAL</b>                              | <b>102.34</b>    | <b>152.10</b>    | <b>211.51</b>    | <b>279.71</b>    | <b>299.85</b>    |
| <b>CAPITAL BASE</b>                                | <b>151.96</b>    | <b>203.17</b>    | <b>416.82</b>    | <b>390.04</b>    | <b>443.48</b>    |

## Financial Summary - Company

|                                          | Unaudited        |                  |                  |                  |                  |
|------------------------------------------|------------------|------------------|------------------|------------------|------------------|
| <b>INCOME STATEMENT (LKR Million)</b>    | <b>31-Mar-04</b> | <b>31-Mar-05</b> | <b>31-Mar-06</b> | <b>31-Mar-07</b> | <b>31-Dec-07</b> |
| Interest Income                          | 339.94           | 376.71           | 453.88           | 586.78           | 579.22           |
| Less: Amortisation Of Premium/(Accretio  | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Less: Net Interest Suspended             | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Less: Interest Expense                   | 217.73           | 211.25           | 240.76           | 334.04           | 381.39           |
| Net Interest Income                      | 122.21           | 165.46           | 213.12           | 252.74           | 197.82           |
| Non-Interest Income                      | 162.21           | 143.83           | 161.12           | 182.83           | 97.57            |
| <b>Gross Income</b>                      | <b>284.42</b>    | <b>309.29</b>    | <b>374.23</b>    | <b>435.57</b>    | <b>295.39</b>    |
| Personnel Expenses                       | 37.68            | 46.96            | 63.55            | 120.34           | 80.73            |
| Other Non-Interest Expenses              | 166.69           | 195.04           | 211.70           | 200.38           | 161.09           |
| Loan Loss Provisions                     | 54.44            | 7.01             | 18.04            | 14.75            | 15.15            |
| Share of results of Associated Companies | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| <b>Pre-Tax Profit</b>                    | <b>25.60</b>     | <b>60.28</b>     | <b>80.95</b>     | <b>100.10</b>    | <b>38.43</b>     |
| Taxation                                 | 0.00             | 5.66             | 13.44            | 32.57            | 6.50             |
| <b>Profit After Tax</b>                  | <b>25.60</b>     | <b>54.63</b>     | <b>67.51</b>     | <b>67.53</b>     | <b>31.93</b>     |
| Extraordinary Items                      | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Prior Year Adjustments                   | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Minority Interests                       | 0.00             | 0.00             | 0.00             | 0.00             | 0.00             |
| Transfer To Statutory Reserves           | 5.10             | 11.00            | 13.60            | 13.50            | 0.00             |
| Transfer To Other Reserves               | 16.45            | 38.75            | 45.70            | 45.93            | 0.00             |
| Dividend                                 | 4.05             | 4.86             | 4.86             | 8.10             | 0.00             |
| <b>Retained Profit For The Year</b>      | <b>0.00</b>      | <b>0.02</b>      | <b>3.35</b>      | <b>0.00</b>      | <b>31.93</b>     |

## Financial Ratios - Company

| KEY RATIOS (%)                               | 31-Mar-04 | 31-Mar-05 | 31-Mar-06 | 31-Mar-07 | 31-Dec-07 |
|----------------------------------------------|-----------|-----------|-----------|-----------|-----------|
| <b>Profitability</b>                         |           |           |           |           |           |
| Net Interest Margin                          | 6.64%     | 7.81%     | 7.84%     | 7.04%     | 6.11%     |
| Non-Interest Income Margin                   | 8.81%     | 6.79%     | 5.93%     | 5.09%     | 3.01%     |
| Cost To Income                               | 71.86%    | 78.24%    | 73.55%    | 73.63%    | 81.86%    |
| Return On Assets                             | 1.39%     | 2.85%     | 2.98%     | 2.79%     | 1.19%     |
| Return On Equity                             | 16.86%    | 31.91%    | 22.47%    | 18.68%    | 9.12%     |
| Dividend Payout                              | 15.82%    | 8.90%     | 7.20%     | 11.99%    | 0.00%     |
| <b>Asset Quality</b>                         |           |           |           |           |           |
| Gross NPL Ratio                              | 12.65%    | 8.94%     | 4.59%     | 3.45%     | 3.31%     |
| Net NPL Ratio                                | 2.45%     | 1.38%     | (0.72%)   | 0.09%     | 0.17%     |
| 3-months Past Due Ratio                      | 21.21%    | 16.68%    | 13.37%    | NA        | NA        |
| Gross NPL Coverage                           | 82.69%    | 85.69%    | 114.76%   | 97.40%    | 94.92%    |
| Loan Loss Reserve Coverage                   | 10.46%    | 7.66%     | 5.27%     | 3.36%     | 3.14%     |
| <b>Liquidity &amp; Funding</b>               |           |           |           |           |           |
| Statutory Liquid Asset Ratio                 | 22.53%    | 18.73%    | 16.02%    | 16.05%    | 15.86%    |
| Customer Deposits To Total Interest Bear     | 89.42%    | 83.37%    | 73.70%    | 68.78%    | 65.70%    |
| Loans To Deposits Ratio                      | 70.27%    | 80.64%    | 109.97%   | 118.56%   | 124.20%   |
| Loans To Stable Funds Ratio                  | 68.47%    | 71.57%    | 82.46%    | 83.57%    | 84.86%    |
| <b>Capital Adequacy</b>                      |           |           |           |           |           |
| Shareholders' Funds To Total Assets          | 8.29%     | 9.46%     | 15.96%    | 14.11%    | 11.83%    |
| Tier 1 Risk Weighted Capital Adequacy Ratio  | 6.33%     | 7.79%     | 8.15%     | 8.01%     | 7.28%     |
| Overall Risk Weighted Capital Adequacy Ratio | 9.41%     | 10.40%    | 12.00%    | 11.16%    | 10.77%    |
| Internal Rate Of Capital Generation          | 51.21%    | 31.99%    | 17.39%    | 11.09%    | 7.58%     |

**Note :**

\* annualised

NA = Not available / Not applicable

## Financial Ratios - Company

| Ratio Definition:-                             |                                                                                                                                                                         |
|------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Net Interest Margin                            | Net Interest Income/Total Average Assets                                                                                                                                |
| Non-Interest Income Margin                     | Non-Interest Income/Total Average Assets                                                                                                                                |
| Cost To Income                                 | Personnel & Other Non-Interest Expenses/Net Interest Income & Non-Interest Income                                                                                       |
| Return On Assets                               | Pre-Tax Profits/Total Average Assets                                                                                                                                    |
| Return On Equity                               | Pre-Tax Profits/Average Shareholders' Funds                                                                                                                             |
| Dividend Payout                                | Dividends/Profit After Tax                                                                                                                                              |
| Gross NPL Ratio                                | (Total Non-Performing Loans - Interest-In-Suspense)/(Gross Loans - Interest-In-Suspense)                                                                                |
| Net NPL Ratio                                  | (Total Non-Performing Loans - Specific Loan Loss Reserves - Interest-In-Suspense)/(Gross Loans - Specific Loan Loss Reserves - Interest-In-Suspense)                    |
| 3-months Past Due                              | 3-months Past Due Loans/(Gross Loans - Interest-in-Suspense)                                                                                                            |
| Specific Loan Loss Provisions For Current Year | Specific Loan Loss Provisions(P&L)/Average Gross Loans                                                                                                                  |
| Gross NPL Coverage                             | General & Specific Loan Loss Reserves (B/S)/(Total Non-Performing Loans - Interest-In-Suspense)                                                                         |
| Loan Loss Reserve Coverage                     | General & Specific Loan Loss Reserves (B/S)/(Gross Loans - Interest-In-Suspense)                                                                                        |
| General Loan Loss Reserve Coverage             | General Loan Loss Reserves/(Gross Loans - Interest-In-Suspense - Specific Loan Loss Reserves)                                                                           |
| Liquid Asset Ratio                             | Liquid Assets/Customer Deposits & Short-Term Funds                                                                                                                      |
| Statutory Liquid Asset Ratio                   | Statutory Liquid Assets/Customer Deposits                                                                                                                               |
| Loans To Deposits                              | Net Loans/Customer Deposits                                                                                                                                             |
| Loans To Stable Funds                          | Net Loans/(Shareholders' Funds + Total Interest Bearing Funds + General Loan Loss Reserves - Interbank Funding - Fixed Assets - Investments in Subsidiaries/Associates) |
| Short-Term Funds                               | Interbank Deposits + Bills & Acceptances + Securities Sold Under Repos                                                                                                  |
| Liquid Assets                                  | Cash & Short-Term Funds + Securities Purchased Under Repos + Deposits & Placements With Financial Institutions + Quoted Securities                                      |
| Statutory Liquid Assets                        | Cash & Short-Term Funds + Securities Purchased Under Repos + Deposits & Placements With Financial Institutions + Government Securities and Treasury Bills               |
| Total Interest Bearing Funding                 | Customer Deposits + Interbank + Bills & Acceptances + Securities Sold Under Repos + Borrowing + Supplementary Capital                                                   |
| Internal Rate Of Capital Generation            | Profit After Tax + Extraordinary Income - Dividend + General Loan Loss Provision/Average Shareholders' Funds                                                            |

## RAM RATINGS' CREDIT RATING DEFINITIONS (FINANCIAL INSTITUTIONS)

RAM Ratings' rating of a financial institution is an assessment and current opinion on the strength and performance of the rated institution.

### LONG-TERM RATINGS

|                                          |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
|------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>AAA</b>                               | Financial institutions rated in this category are adjudged to offer the highest safety for timely payments of financial obligations. This level of rating indicates entities with strong balance sheets, favourable credit profiles and consistent records of above-average profitability. Their capacities for timely payments of contractual financial obligations are unlikely to be impacted seriously by any foreseeable changes in economic conditions.                                                                                                                                                                                                                       |
| <b>AA+</b><br><b>AA</b><br><b>AA-</b>    | Financial institutions rated in this category are adjudged to offer high safety for timely payments of financial obligations. This level of rating indicates entities with sound credit profiles and without significant problems. Entities rated in this category are, however, considered to be somewhat more vulnerable to adverse changes in economic conditions than those entities rated in the highest category. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.                                                                                      |
| <b>A+</b><br><b>A</b><br><b>A-</b>       | Financial institutions rated in this category are adjudged to offer adequate safety for timely payments of financial obligations. This level of rating indicates entities with adequate credit profiles, but which possess one or more problem areas, giving rise to the possibility of future riskiness. Entities rated in this category have generally performed at industry average and are considered to be more vulnerable to changes in economic conditions than those rated in the higher categories. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively. |
| <b>BBB+</b><br><b>BBB</b><br><b>BBB-</b> | Financial institutions rated in this category are adjudged to offer only a moderate degree of safety for timely payments of financial obligations. This level of rating indicates entities which have been significantly under-performing in some areas. These entities are, however, considered to have the capability to overcome such problems in the short term, though adverse changes in economic conditions could impair their ability to make timely payments of financial obligations. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.              |
| <b>BB+</b><br><b>BB</b><br><b>BB-</b>    | Financial institutions rated in this category are adjudged to lack key protection factors, which could result in inadequate safety for timely payments of financial obligations. This level of rating indicates that the entities may need certain favourable economic changes in order to meet financial obligations in a timely fashion. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.                                                                                                                                                                   |
| <b>B+</b><br><b>B</b><br><b>B-</b>       | Financial institutions rated in this category are adjudged to be of high risk. Timely payments of financial obligations are impaired by serious problems which the entities face. Whilst entities rated in this category might be currently meeting obligations on time, continuance of this would depend upon favourable economic conditions or some degree of external support. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.                                                                                                                            |
| <b>C+</b><br><b>C</b><br><b>C-</b>       | Financial institutions rated in this category are adjudged to be of very high risk in relation to timely payments of financial obligations. This level of rating indicates entities with very serious problems and, unless external support is provided, they would be unable to meet their financial obligations in a timely fashion. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.                                                                                                                                                                       |
| <b>D</b>                                 | Financial institutions rated in this category are either currently in default or expected to be in default, whether or not formally declared. This level of rating indicates that the entities are unlikely to meet maturing financial obligations, which calls for immediate external support of a high order.                                                                                                                                                                                                                                                                                                                                                                     |

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## SHORT-TERM RATINGS

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- P1** Financial institutions in this category have superior capacities for timely payments of obligations.
- P2** Financial institutions in this category have strong capacities for timely payments of obligations.
- P3** Financial institutions in this category have adequate capacities for timely payments of obligations. The ability to honour the obligations is more vulnerable to adverse changes in business, economic or financial conditions.
- NP** Financial institutions in this category have doubtful capacities for timely payments of obligations.

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