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Media Release

RAM Ratings Lanka upgrades Citizens Development Business Finance PLC's ratings to BBB/P2 with a stable outlook

RAM Ratings Lanka has upgraded the respective long- and short-term financial institution ratings of Citizens Development Business Finance PLC ("CDB" or "the Company"), from BBB- and P3 to BBB and P2. At the same time, we have also upgraded the long-term rating of CDB's LKR 250 million Unsubordinated Unsecured Redeemable Unlisted Debentures, from BBB- to BBB. The outlook on the long-term ratings is stable. The rating upgrade reflects the Company's improving asset-quality indicators and strengthened capitalisation following an equity infusion in August 2011.

CDB's ratings continue to be supported by its healthy asset quality as well as its improving financial performance and market share. On the other hand, the ratings are pressured by its weak operational efficiencies, as reflected by its high cost-to-income ratio. CDB is a medium-sized registered finance company ("RFC"), accounting for 5.06% of the industry's assets as at end-March 2011 (end-March 2010: 3.40%).

The Company's loan book expanded a robust 54.90% year-on-year ("y-o-y") in FYE March 2011 ("FY Mar 2011"), compared with the industry's 42.29%. The momentum followed through to 1H FY Mar 2012, when its loan portfolio came up to LKR 10.38 billion as at end-September 2011 (end-FY Mar 2011: LKR 7.88 billion). The expansion had been achieved through CDB's network of 31 branches nationwide, with emphasis on high-growth segments such as 3-wheeler financing and pawning. Simultaneously, the Company had also focused on improving its asset quality by strengthening its monitoring and recovery procedures, leading to better collections. Accordingly, CDB managed to rein in its absolute gross non-performing loans ("NPLs"), which eased to LKR 285.54 million as at end-September 2011 from a high of LKR 396.29 million as at end-FY Mar 2010. In tandem with its reduced NPLs and enlarged base of credit assets, CDB's gross NPL ratio eased from 7.49% to 2.72% over the same span; this is better than those of its similar rated peers. Nevertheless, we acknowledge that the Company's loan portfolio lacks seasoning due to its aggressive loan growth of late.

Meanwhile, CDB's performance has been improving. The Company's interest income leapt 41.42% y-o-y in 1H FY Mar 2012, supported by its expanding loan portfolio. However, its net interest margin ("NIM") contracted slightly to 9.35% (FY Mar 2011: 9.69%) owing to the downward repricing of its loans. All said, the Company's NIM is still broader than those of its similar rated peers. On the other hand, its cost-to-income ratio remained weaker than its peers' as a result of its

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aggressive branch expansion. Nonetheless, the ratio had improved slightly to 64.16% as at end-1H FY Mar 2012 (end-fiscal 2011: 67.07%, excluding mark-to-market adjustments on investment securities).

On a separate note, RAM Ratings Lanka opines that CDB's funding and liquidity positions are adequate. The Company's funding base is dominated by deposits and further supported by increased long-term borrowings. This, together with more shorter-tenured, small-ticket loans, has partially addressed the Company's asset-liability maturity mismatches ("ALMM"). However, CDB's loans-to-deposits ("LD") ratio clocked in at 109.69% as at end-1H FY Mar 2012, albeit better than those of its similar rated peers; its statutory liquid-asset ratio stood at 13.05% (end-fiscal 2011: 13.51%) - broadly in line with its peers'.

Meanwhile CDB's capitalisation is deemed good, strengthened by an equity infusion of LKR 718 million in August 2011. As a result, its tier-1 and overall risk-weighted capital-adequacy ratios ("RWCARs") had improved to 15.65% and 16.32%, respectively, by end-1H FY Mar 2012 (end-fiscal 2011: 12.23% and 12.46%) - better than those of its similar rated peers. CDB's internal capital-generation ratio of 31.05% is also better than its peers'.

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