

RAM

RATINGS

CREDIT RATING RATIONALE

FINANCIAL INSTITUTIONS – SRI LANKA

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

Mercantile Investments Limited – new issue & credit update

Financial Institution**Ratings:**

Long-term: A [Reaffirmed]
Short-term: P1 [Reaffirmed]

Rating Outlook:

Negative

Instruments:

(i) Proposed LKR 100 million 3-month commercial paper ("CP")

(ii) LKR 250 million 3-month CP

Ratings:

(i) P1 [Assigned]
(ii) P1 [Reaffirmed]

Tenures:

(i) 3-month CP revolving up to 15 months, LKR 20 million repayable quarterly
(ii) 3-month CP revolving up to 15 months, LKR 50 million repayable quarterly

Coupon Rates:

(i) Average of past 3 months' AWPLR + 2.30% per annum
(ii) Average of past 3 months' AWPLR + 2.25% per annum

Strengths:

- Sturdy capitalisation
- Adequate liquidity

Weaknesses:

- Declining profitability
- Weak asset quality

Principal Activities:

Finance company engaged in hire-purchase, leasing, loans and accepting public deposits

Analysts:

Prakash Jerome ACMA ASCMA
(9411) 2503551
prakash@lankarating.com

Summary

RAM Ratings has assigned a short-term rating of P1 to Mercantile Investments Limited's ("MIL" or "the Company") proposed LKR 100 million commercial paper ("CP") programme. Concurrently, RAM Ratings has reaffirmed the Company's respective long- and short-term financial institution ratings of A and P1. At the same time, the P1 rating of MIL's outstanding LKR 250 million CP programme has also been reaffirmed.

MIL's ratings are supported by its sturdy capitalisation and adequate liquidity position. The assigned rating is at par with MIL's short-term financial institution rating, as the proposed issuance ranks *pari passu* with the Company's other senior unsecured creditors. However, the outlook on its long-term rating remains negative, as its financial performance and asset quality have stayed soft; the short term rating is however unlikely to change unless there is a drastic deterioration in liquidity and funding.

MIL is the fourth-largest finance company in Sri Lanka, accounting for approximately 6% of the industry's assets as at the end of FYE 31 March 2008 ("FY Mar 2008"). Meanwhile, the local industry is concentrated, with the 2 biggest players taking up over 50% of the industry's assets. Against this backdrop, MIL has built its franchise throughout its 44-year history, primarily as an importer, trader and financier of motor vehicles. In the past few years, the competition in the industry has been intensifying with commercial banks venturing into the leasing sector. To mitigate the effects of competition to some extent, MIL - like other registered finance companies ("RFCs") - is expanding its branch network. The Company had 2 branches as at end-FY Mar 2008, and added 2 more by June this year.

Historically, MIL has been one of the most profitable RFCs in Sri Lanka, having enjoyed returns on assets ("ROA") of over 6%. As interest rates rose, however, the Company's interest expenses also elevated in tandem; the improving trend in its asset quality had thus reversed, resulting in a sharp fall in the Company's ROA, which only came up to 2.95% as at end-FY Mar 2008 (end-FY Mar 2007: 4.92%).

By end-June 2008, however, MIL's tightening collections and recoveries began to bear fruit. The Company's gross non-performing-loan ("NPL") ratio, though still weaker than the industry average, eased slightly from 7.64% as at end-FY Mar 2008 to 7.58%. In absolute terms, its gross NPLs contracted from LKR 432.68 million to LKR 417.30 million over the same period. Going forward, the management intends to remain focused on recoveries while expanding its loan books, albeit at a conservative pace.

Shivanthi Sugathadasa
BSc, ACMA
(9411) 2553089
shivanthi@ram.com.lk

Company Contact:

Priya Thamotheram
FCA, FCMA, FSCMA
Chief Executive Officer
(9411) 2596099
priya@ram.com.lk
Website: www.ram.com.lk

In line with its improving asset quality, MIL's liquidity and funding levels have also ameliorated. The Company's statutory liquidity ratio, which stood at 17.28% as at end-FY Mar 2008, climbed up to 17.65% as at end-June 2008. Concurrently, its loans-to-deposits ratio eased from 223.38% to 203.43% over the same span, as a larger share of funding had stemmed from public deposits.

RAM Ratings notes that MIL's capitalisation is still its key rating driver, with an impressive tier-1 capital-adequacy ratio of 20.83% as at end-June 2008. RAM Ratings draws confidence from the fact that the Company's robust capitalisation had been build-up primarily by prudent retention of profits. In additions, the Company's effective recovery efforts have also improved; its ratio of net NPLs to shareholders' funds descended from 5.60% as at end-FY Mar 2008 to 3.58% as at end-June 2008.

Going forward, MIL intends to augment its loan base at a conservative pace, so as to maintain its asset quality. Meanwhile, it also plans to partially mitigate interest-rate risk by tapping public deposits and curtailing short-term, high-interest borrowings. RAM Ratings will monitor the Company's progress in this regard and take the appropriate rating action as and when warranted.

Outlook

The negative outlook on MIL's long-term rating reflects the Company's deteriorating profit performance and weaker-than-average asset quality. The continuation of this trend will exert downward pressure on the Company's existing ratings. The Company's short term rating of P1 is unlikely to be impacted, unless there is a sharp deterioration in liquidity and funding.

While an upward movement in MIL's long term rating is unlikely, its outlook may be reinstated to stable if its asset quality demonstrates sustainable improvement while revisiting historical performance levels.

Industry Overview

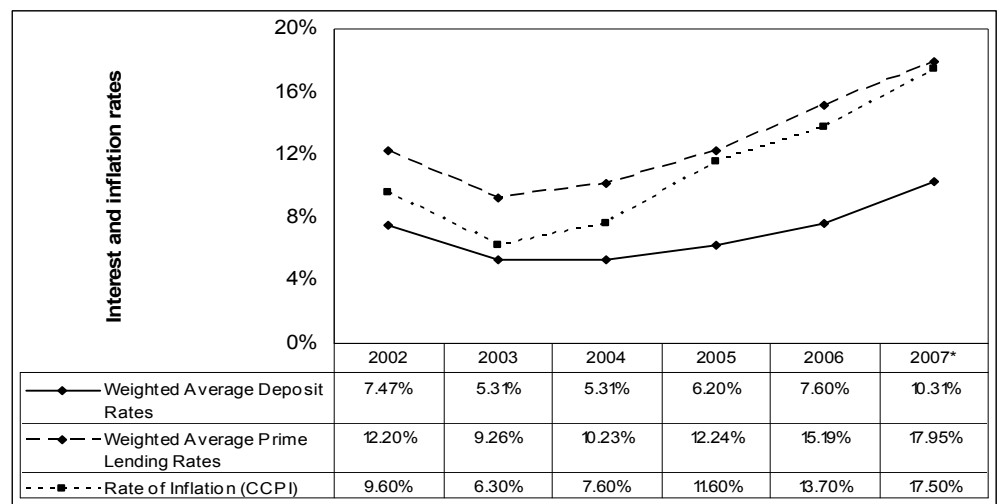
Sri Lanka’s gross domestic product (“GDP”) is estimated to have expanded by 6.8% in 2007 (2006: +7.7%). Growth had slowed down for all sectors, with agriculture and services recording the most acute deceleration (refer to Table 2). All sub-segments within the services sector had lost momentum, with the 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 2: 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% |
| Total | 7.7% | 6.8% |

The domestic banking sector, meanwhile, had progressed despite rising interest rates driven by housing and consumption loans. Greater inflation is likely to have propelled 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 8). Against this backdrop, the weighted-average deposit rate¹ has been lower than the inflation rate, resulting in negative real returns for depositors.

Chart 8: Trends in interest and inflation rates



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

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

¹ 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.

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

| | |
|---|---|
| <p>Liquid assets</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"> a) Cash in hand. b) Balances in a current or deposit account in a commercial bank, free from any banker's lien or charge. c) Sri Lankan Government Treasury Bills, free from any charge or lien. d) Sri Lankan Government Securities maturing within 1 year and free from any charge or lien. e) Central Bank securities maturing within 1 year and free from any charge or lien. f) Cash balance, if any, maintained with the Central Bank. <p>The minimum limits are as follows:</p> <ol style="list-style-type: none"> 1. For time deposits, 15% of outstanding deposits. 2. For certificates of deposits, 15% of the face value of the certificates. 3. For savings deposits, 20% of the outstanding deposits. <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>Provision of bad and doubtful debts</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"> (a) 50% of all advances in arrears for a period of 7 to 12 months. (b) 100% of all advances in arrears for 13 months or more. <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"> 1. The value so deducted should not exceed the value decided by a professional valuer at the time of granting the advance. 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. <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"> (a) 50% of all advances in arrears for a period of 12 to 24 months. (b) 100% of all advances in arrears for more than 24 months. <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> <ul style="list-style-type: none"> (a) 50% of all advances in arrears for a period of 6 to 12 months. (b) 100% of all advances in arrears for 13 months or more. <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"> 1. Sri Lankan Government securities, free from any lien or charge. 2. Central Bank securities, free from any lien or charge. 3. Time deposits in a licensed commercial bank, specialised bank or RFC, free from any lien or charge. 4. Bank guarantees. 5. With regard to repossessed vehicles and machinery, 80% of the valuation obtained in the preceding 6 months and by an approved valuer. 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"> a) 6-36 months, 100% of the value is deductible b) 37-60 months, 80% of the value is deductible c) 61-120 months, 50% of the value is deductible d) more than 120 months, 0% of the value is deductible |
| <p>Capital adequacy</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> <ul style="list-style-type: none"> (a) Tier I - Core Capital <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> <ul style="list-style-type: none"> (b) Tier II - Supplementary Capital <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>Single-borrower limit</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>Minimum core-capital requirement</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> <p>(a) A finance company with a core capital of less than LKR 100 million must:</p> <ol style="list-style-type: none"> 1. enhance its core capital to at least LKR 100 million by February 2007; and 2. bring the remaining LKR 100 million or the deficit up to the core-capital requirement of LKR 200 million by July 2008. <p>(b) A finance company with a core capital of between LKR 100 million and LKR 200 million must bring in:</p> <ol style="list-style-type: none"> 1. at least 50% of the deficient amount to meet the core-capital requirement of LKR 200 million by February 2007; and 2. the balance of the deficient amount up to the core capital requirement of LKR 200 million by July 2008. |
| <p>Investments</p> | <p>A finance company must not invest in the shares of any company</p> <p>(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</p> <p>(b) In aggregate, in excess of 25% of the capital funds of the finance company</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> |

Corporate Information

Date of Incorporation: 1964

Commencement of Business: 1964

Major Shareholders:

| | |
|-------------------------------|--------|
| Mr GLA Ondaatjie | 51.07% |
| Nilaveli Beach Hotels Ltd | 20.83% |
| Mercantile Fortunes (Pvt) Ltd | 13.67% |
| Tangerine Tours Ltd | 6.67 % |
| Mr GG Ondaatjie | 1.67 % |
| Ms AM Ondaatjie | 1.67 % |
| Mr TJ Ondaatjie | 1.67 % |
| Mr GV Divitawela | 0.83 % |
| Mr JS Dominic | 0.50 % |
| Mr RMD Abeygunawardena | 0.33 % |

Directors:

| | |
|--------------------------------------|------------------------------|
| Deshabandu G L Andrew Ondaajie | Chairman & Managing Director |
| Mr Gerard George Ondaatjie | Executive Deputy Chairman |
| Mr Shermal Hemaka Jayasuriya | Finance Director |
| Mrs Mignonne Bernadette Assuaw | Director Deposits |
| Mr Pathiranage Mahes Amarasekera | Director Recoveries |
| Mr Saman Kumara Abraham Galappaththi | Director Legal |
| Mrs Angeline Myrese Ondaatjie | Director |
| Mr Travis John Ondaatjie | Director |
| Mr Justin Severimuttu Dominic | Director |

Auditor: Cecil Arsecularatne & Co (External Auditors)
SJMS Associates (Internal Auditors)

Listing: Not listed

Key Management:

| | |
|----------------------------------|---------------------------|
| Mr Gerard George Ondaatjie | Executive Deputy Chairman |
| Mr Shermal Hemaka Jayasuriya | Finance Director |
| Mrs Mignonne Bernadette Assuaw | Director Deposits |
| Mr Pathiranage Mahes Amarasekera | Recoveries Director |

Major Subsidiaries and Associates:

Tangerine Beach Hotels Ltd, Nuwara Eliya Hotels Co Ltd,
Royal Palms Beach Hotels Ltd, Nilaveli Beach Hotels Ltd,
Tangerine Tours Ltd, Mercantile Fortunes (Pvt) Ltd

Capital History:

| Year | Remarks | Amount (LKR million) | Cumulative Total (LKR million) |
|------|-----------------|-------------------------|--------------------------------------|
| 1964 | First allotment | 0.07 | 0.07 |
| 1965 | Issue of shares | 0.07 | 0.14 |
| 1966 | Issue of shares | 0.07 | 0.21 |
| 1966 | Issue of shares | 0.03 | 0.24 |
| 1967 | Issue of shares | 0.01 | 0.25 |
| 1967 | Issue of shares | 0.24 | 0.49 |
| 1967 | Issue of shares | 0.01 | 0.50 |
| 1982 | Issue of shares | 0.50 | 1.00 |
| 1988 | Bonus Issue | 1.00 | 2.00 |
| 1989 | Bonus Issue | 1.00 | 3.00 |
| 1989 | Bonus Issue | 2.00 | 5.00 |
| 1993 | Issue of shares | 5.00 | 10.00 |
| 1995 | Bonus Issue | 10.00 | 20.00 |
| 1997 | Issue of shares | 5.00 | 25.00 |
| 2004 | Issue of shares | 5.00 | 30.00 |

Financial Summary - Company

unaudited

| BALANCE SHEET (LKR Million) | 31-Mar-05 | 31-Mar-06 | 31-Mar-07 | 31-Mar-08 | 30-Jun-08 |
|--|------------------|------------------|------------------|------------------|------------------|
| ASSETS | | | | | |
| Cash & Money At Call | 38.96 | 90.40 | 71.63 | 71.81 | 89.35 |
| Deposits & Placements With Financial Institutions | 0.00 | 51.42 | 100.00 | 104.10 | 108.47 |
| Securities Purchased Under Resale Agreements | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Securities | | | | | |
| Dealing Securities | 516.30 | 570.51 | 628.38 | 688.02 | 709.43 |
| Investment Securities | 5.22 | 3.27 | 3.27 | 2.46 | 2.40 |
| Gross Loans & Advances | 3,582.98 | 4,761.22 | 5,402.40 | 6,093.08 | 6,098.90 |
| Interest-In-Suspense | 201.33 | 245.04 | 312.83 | 430.43 | 473.80 |
| General Loan Loss Reserves | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Specific Loan Loss Reserves | 216.94 | 227.53 | 237.65 | 280.75 | 327.82 |
| Net Loans & Advances | 3,164.70 | 4,288.65 | 4,851.93 | 5,381.90 | 5,297.28 |
| Investments in Subsidiaries/Associates | 623.86 | 671.77 | 751.63 | 749.16 | 749.16 |
| Investment Land and Properties | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Other Assets | 116.83 | 156.59 | 242.19 | 263.99 | 323.02 |
| Property, Plant and Equipment | 376.76 | 367.23 | 859.20 | 888.38 | 889.32 |
| TOTAL ASSETS | 4,842.63 | 6,199.81 | 7,508.23 | 8,149.80 | 8,168.42 |
| LIABILITIES | | | | | |
| Customer Deposits | | | | | |
| Savings | 0.00 | 0.00 | 0.00 | 7.57 | 0.00 |
| Fixed | 1,533.10 | 1,701.15 | 1,959.14 | 2,246.69 | 2,603.93 |
| NIDs | 85.90 | 109.90 | 106.50 | 155.00 | 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 Agreements | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Other Borrowing | 1,176.61 | 2,014.35 | 2,265.37 | 2,444.54 | 2,189.97 |
| Subordinated Debt & Hybrid Capital | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Other Liabilities | 244.17 | 373.08 | 593.99 | 583.95 | 614.35 |
| TOTAL LIABILITIES | 3,039.77 | 4,198.48 | 4,925.00 | 5,437.74 | 5,408.26 |
| Paid-up Capital | 30.00 | 30.00 | 30.00 | 30.00 | 30.00 |
| Minority Interest | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Share Premium & Other Reserves | 1,564.97 | 1,713.21 | 2,273.33 | 2,380.64 | 2,380.64 |
| Statutory General Reserve | 206.40 | 256.40 | 276.40 | 296.40 | 296.40 |
| Retained Profits/(Loss) | 1.49 | 1.72 | 3.50 | 5.02 | 53.13 |
| Total Shareholders' Funds | 1,802.86 | 2,001.33 | 2,583.22 | 2,712.06 | 2,760.17 |
| TOTAL LIABILITIES & SHAREHOLDERS' FUNDS | 4,842.63 | 6,199.81 | 7,508.23 | 8,149.80 | 8,168.42 |
| COMMITMENTS & CONTINGENCIES | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| TIER 1 CAPITAL | 1,187.30 | 1,332.50 | 1,414.33 | 1,548.85 | 1,596.96 |
| CAPITAL BASE | 1,495.08 | 1,666.89 | 1,998.77 | 2,130.45 | 2,178.56 |

Financial Summary - Company

| | unaudited | | | | |
|---|------------------|------------------|------------------|------------------|------------------|
| INCOME STATEMENT (LKR Million) | 31-Mar-05 | 31-Mar-06 | 31-Mar-07 | 31-Mar-08 | 30-Jun-08 |
| Interest Income | 700.04 | 889.69 | 1,025.59 | 1,307.42 | 359.90 |
| Less: Amortisation Of Premium/(Accretion Of Discount) | 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 | 241.25 | 335.39 | 447.07 | 720.13 | 221.95 |
| Net Interest Income | 458.79 | 554.30 | 578.52 | 587.29 | 137.95 |
| Non-Interest Income | 99.45 | 84.81 | 66.74 | 64.72 | 19.83 |
| Gross Income | 558.24 | 639.10 | 645.27 | 652.01 | 157.78 |
| Personnel Expenses | 80.99 | 95.20 | 111.68 | 134.48 | 33.76 |
| Other Non-Interest Expenses | 142.27 | 170.08 | 177.50 | 234.19 | 39.75 |
| Loan Loss Provisions | 23.00 | 13.04 | 18.77 | 52.05 | 36.17 |
| Share of results of Associated Companies | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Pre-Tax Profit | 311.98 | 360.78 | 337.31 | 231.29 | 48.11 |
| Taxation | 7.03 | 77.10 | 100.33 | 82.72 | 0.00 |
| Profit After Tax | 304.95 | 283.69 | 236.99 | 148.57 | 48.11 |
| Extraordinary Items | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Prior Year Adjustments | 0.00 | 0.00 | (95.13) | 0.00 | 0.00 |
| Minority Interests | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Transfer To Statutory Reserves | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Transfer To Other Reserves | 265.00 | 254.14 | 80.00 | 133.00 | 0.00 |
| Dividend | 42.19 | 29.32 | 60.08 | 14.05 | 0.00 |
| Retained Profit For The Year | (2.24) | 0.23 | 1.78 | 1.52 | 48.11 |

Financial Ratios - Company

| KEY RATIOS (%) | 31-Mar-05 | 31-Mar-06 | 31-Mar-07 | 31-Mar-08 | 30-Jun-08 |
|---|-----------|-----------|-----------|-----------|-----------|
| Profitability | | | | | |
| Net Interest Margin | 11.34% | 10.04% | 8.44% | 7.50% | 6.76% |
| Non-Interest Income Margin | 2.46% | 1.54% | 0.97% | 0.83% | 0.97% |
| Cost To Income | 39.99% | 41.51% | 44.82% | 56.54% | 46.59% |
| Return On Assets | 7.71% | 6.53% | 4.92% | 2.95% | 2.36% |
| Return On Equity | 20.63% | 18.97% | 14.72% | 8.74% | 6.85% |
| Dividend Payout | 13.83% | 10.34% | 25.35% | 9.46% | 0.00% |
| Asset Quality | | | | | |
| Gross NPL Ratio | 8.75% | 6.83% | 6.05% | 7.64% | 7.58% |
| Net NPL Ratio | 2.49% | 1.88% | 1.45% | 2.82% | 1.86% |
| Specific Loan Loss Provisions For Current Year | 0.76% | 0.31% | 0.37% | 0.91% | 2.37% |
| Gross NPL Coverage | 73.34% | 73.82% | 77.16% | 64.90% | 76.86% |
| Loan Loss Reserve Coverage | 6.42% | 5.04% | 4.67% | 4.96% | 5.83% |
| General Loan Loss Reserve Coverage | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Liquidity & Funding | | | | | |
| Liquid Asset Ratio | 28.08% | 31.87% | 27.56% | 24.40% | 29.45% |
| Statutory Liquid Asset Ratio | 17.86% | 19.63% | 17.52% | 17.28% | 17.65% |
| Customer Deposits To Total Interest Bearing Funds | 57.91% | 47.34% | 47.69% | 49.64% | 54.32% |
| Loans To Deposits Ratio | 195.47% | 236.80% | 234.89% | 223.38% | 203.43% |
| Loans To Stable Funds Ratio | 87.96% | 89.58% | 91.49% | 90.78% | 89.55% |
| Capital Adequacy | | | | | |
| Shareholders' Funds To Total Assets | 37.23% | 32.28% | 34.41% | 33.28% | 33.79% |
| Tier 1 Risk Weighted Capital Adequacy Ratio | 26.22% | 22.81% | 19.79% | 20.06% | 20.83% |
| Overall Risk Weighted Capital Adequacy Ratio | 33.02% | 28.53% | 27.96% | 27.59% | 28.41% |
| Internal Rate Of Capital Generation | 17.38% | 13.37% | 7.72% | 5.08% | 6.85% |

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

| | |
|--|---|
| AAA | 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. |
| AA+ AA AA- | 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. |
| A+ A A- | 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. |
| BBB+ BBB BBB- | 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. |
| BB+ BB BB- | 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- | 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. |
| C+ C C- | 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. |
| D | 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. |

SHORT-TERM RATINGS

- 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.

This page has been intentionally left blank

Published by RAM Ratings.
Reproduction or transmission in any form is prohibited
except by permission from RAM Ratings.

RAM Ratings (Lanka) Limited
No. 9 Arthur's Place
Colombo 4
Sri Lanka

Tel: (9411) 2553089 Fax: (9411) 2553090

E-mail: ram@ram.com.lk
Website: <http://www.ram.com.lk>

