RAM

# CREDIT RATING RATIONALE

November 2011

## ARPICO FINANCE COMPANY PLC

- Financial Institution Ratings

RAM Ratings (Lanka) Ltd

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RAM RATINGS

# CREDIT RATING RATIONALE

## FINANCIAL INSTITUTION RATINGS

**NOVEMBER 2011**


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**Principal Activities:**
Finance company engaged in hire-purchase, leasing, retail loans and acceptance of public deposits.

**Ratings:**
Long-term: BB (Reaffirmed)
Short-term: NP (Reaffirmed)

**Rating Outlook:**
Positive

**Previous Ratings:**
Long-term: BB
Short-term: NP

**Last Rating Action:**
October 2010

## ARPICO FINANCE COMPANY PLC – Rating Review

### Summary


RAM Ratings Lanka has reaffirmed the respective long- and short-term financial institution ratings of Arpico Finance Company PLC (“Arpico” or “the Company”), at BB and NP; the long-term rating has a positive outlook. Arpico’s ratings are supported by its good asset quality as well as adequate performance and capitalisation. Nevertheless, the ratings are moderated by the Company’s small stature and high cost-to-income ratio relative to its similarly rated peers. The positive outlook on the long-term rating, meanwhile, reflects the uptrend in Arpico’s profitability and asset-quality indicators. The outlook had been revised from stable to positive in 2010, premised on Arpico’s improved asset-quality indicators relative to its peers.

Arpico remains a small registered finance company (“RFC”) in Sri Lanka, accounting for only 0.86% of the industry’s assets as at end-March 2011. The Company is the second-oldest RFC in the country, with a 60-year operating history; it enjoys a good reputation and brand name derived from its former parent.

The Company’s asset quality is deemed good. Its loan assets augmented 29.16% year-on-year (“y-o-y”) in FYE 31 March 2011 (“end-FY Mar 2011”), supported by new branches and initiatives to strengthen its presence in high-growth segments such as 3-wheelers and pawn broking. Nonetheless, Arpico’s loans had expanded at a slower pace than the industry’s 42.29%. Meanwhile, the Company’s non-performing loans (“NPLs”) climbed LKR 18.11 million to LKR 84.25 million as at end-FY Mar 2011, driven by the strong loan growth and the fact that new loans had yet to be sufficiently seasoned. However, its gross NPL ratio eased from 3.51% as at end-FY Mar 2010 to 3.32% as at end-FY Mar 2011. While this was mainly anchored by its robust accretion of credit assets, Arpico had been able to maintain a better gross NPL ratio over the period.

We note that Arpico's performance improved in FY Mar 2011, underpinned by a surge in net interest income that was supported by loan expansion and lower funding costs due to the faster repricing of deposits relative to its fixed-rate hire-purchase ("HP") and leasing loans amid the environment of tapering interest rates. As such, its net interest margin ("NIM") widened from 6.77% to 9.68% y-o-y. While the Company's operating expenses also climbed up 36.14% y-o-y amid its branch expansion, these were offset by the surge in gross income from its newly opened pawning centres and the branch, which had broken even within 9 months. As a result, its cost-to-income ratio had also eased from 94.35% to 82.21%. That said, this remained weaker than those of Arpico's similar rated peers as most of its operations had been undertaken manually; the Company is in the process of implementing a new information-technology ("IT") system.

Moving ahead, RAM Ratings Lanka anticipates Arpico's loan expansion to drive its top-line growth over the medium term. Nevertheless, we expect its overheads to increase in line with its anticipated branch expansion; this may dampen its bottom-line growth until the new branches break even.

Arpico's funding and liquidity levels are deemed moderate. Its funding base is dominated by deposits and further supported by long-term borrowings. The Company's loans-to-deposits ("LD") ratio climbed up from 108.77% as at end-FY Mar 2010 to 112.62% a year later, reflecting its robust loan expansion relative to deposit growth - a general trend across the RFC industry. Furthermore, Arpico's liquidity levels has diminished as a result of channelling its funds to fuel the loan growth; its statutory liquid-asset ratio reduced to 12.87% as at end-FY Mar 2011 (FY Mar 2010: 18.20%).

Meanwhile, Arpico's capital cushioning is deemed adequate. Its tier-1 and overall risk-weighted capital-adequacy ratio ("RWCAR") clocked in at a respective 13.91% and 16.06% as at end-FY Mar 2011, providing sufficient buffer for steady loan growth. Nevertheless, Arpico is required to enlarge its capital base from LKR 235.69 million (as at end-FY Mar 2011) to LKR 300 million by end-December 2012, in accordance with the Central Bank of Sri Lanka's ("CBSL") regulations, which the Company intends to meet via internal capital generation.

We highlight that the ratings may be upgraded if Arpico can improve its market share while demonstrating its ability to maintain its asset quality as well as to increase profitability to remain better than similar-rated peers. Conversely, the outlook may be revised to stable if Arpico's asset-quality indicators show deterioration.

## Company Background

***Small RFC despite long history***

Established in 1951, Arpico comes under the regulatory purview of the CBSL as an RFC and is governed by the Finance Companies Act No. 78 of 1988. The Company is the second-oldest RFC in Sri Lanka and is listed on the Colombo Stock Exchange ("CSE"). Despite its 60-year operating history, Arpico has remained a small player, accounting for only 0.86% of the industry's assets as at end-FY Mar 2011 (end-FY Mar 2010: 0.87%).

***New branches planned***

Headquartered in Colombo, the Company operates with 2 branches; it plans to open 3 new outlets in Mulativu, Godagama and Minuwangoda by end-FY Mar 2012. In addition, Arpico had opened 2 pawning centres during fiscal 2011 which increased its pawning network to 8 outlets. The Company mainly derives its income from the provision of leasing and HP facilities. On the funding side, it accepts deposits from the public.

***Part of Alliance Group***

Following capital infusions in FY Mar 2009, Alfinco Insurance Brokers (Pvt) Ltd became the major shareholder of Arpico accounting for 40.56% of its shares. Despite the change in its shareholding structure, Arpico is still under the Alliance Group's umbrella. Both Arpico and Alliance Finance PLC (rated at BBB/stable/P2 by RAM Ratings Lanka) are chaired by Mr Pratapkumar de Silva, a veteran in the RFC sector.

## Management & Strategies

***Senior management unchanged***

Arpico's operations fall under the purview of Joint Managing Director Mr Senakke Bandaranayake, Finance Director Mr Bede Jayalath, and Legal Director Ms Ruvini Weerasinghe.

***Branching out***

The management intends to extend Arpico's geographical reach by opening 3 new outlets in fiscal 2012, bringing its total count to 5. Notably, a new branch will be located in Mulativu, with the aim of establishing its presence in the Northern Province, from which high growth potential is foreseen after the end of country's 30-year ethnic conflict.

***Concentration on lease and HP facilities***

We positively view the management intentions of steadily expanding its credit assets, as opposed to the situation of many other RFCs that have expanded aggressively. Although Arpico will remain focused on leasing and HP facilities, we expect the former to grow faster, supported by high-yielding 3-wheeler financing over the medium term. While the management intends to expedite loan-disbursement procedures by decentralising the approval process, Arpico has defined approval limits for different management levels, in an effort to preserve its underwriting standards.

***Pawn broking to gain prominence***

Arpico has also strengthened its presence in pawning by increasing its outlet count to 8 as at end-FY Mar 2011. Given the rising demand for pawning services, this sector is expected to aid the Company expand its credit portfolio and earnings, on account of its broader margins. To enlarge its pawning portfolio, the management plans to promote the product with a new pricing structure. It has also appointed a new general manager to overlook the segment while strengthening the marketing team.

***New IT system***

Arpico is in the process of implementing a new IT system, which is expected to be completed in the near to medium term. Thus far, its client ledgers, deposit acceptance and recovery procedures have been processed via this system, thereby addressing major operational issues the Company had faced with its previous manual operations. This new IT system is expected to curtail its operational expenses and facilitate branch expansion with a high level of integration.

## ■ Corporate Governance

***Change in board composition***

The Company appointed a new non-executive director to its board; it presently has 7 directors, of whom 4 are in a non-executive capacity. The board, which convenes monthly to review the Company's performance, is further supported by several committees: audit, remuneration, integrated risk management as well as recoveries.

## ■ Asset Quality

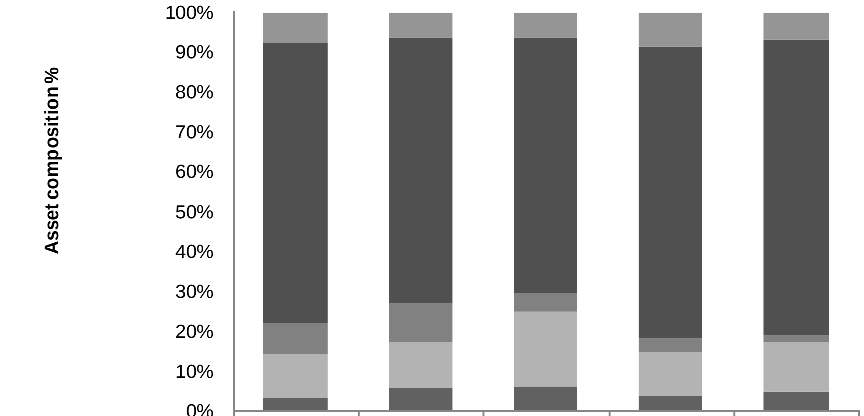
***Good asset quality***

The Company's asset quality is deemed good, as reflected in its indicators which stood on par with those of its similar-rated peers. Its gross NPL ratio had eased to 3.23% as at end-FY Mar 2011, from 3.51% a year earlier, supported by the robust expansion of its loan book. Nevertheless, RAM Ratings Lanka's concerns hinge on Arpico's relatively unseasoned credit portfolio, which increases the possibility of delinquencies as the loan book seasons. However, we derive comfort from Arpico's focus on loan products with relatively low default rates.

***Loans driving asset-base growth***

Arpico's asset base enlarged 26.69% y-o-y to LKR 1.41 billion as at end-FY Mar 2011. This was anchored by the robust expansion of the Company's credit assets, which surged 29.16% y-o-y amid the improving economic landscape, supported by new branches and pawning centres. Accordingly, credit assets continued to dominate its asset base (refer to Chart 1). Meanwhile, the proportion of real-estate assets was reduced to 1.58% as at end-FY Mar 2011, due to the rising prominence of its loan assets and the management's intention of discontinuing that segment while disposing of its remaining land bank.

**Chart 1: Arpico's asset composition**



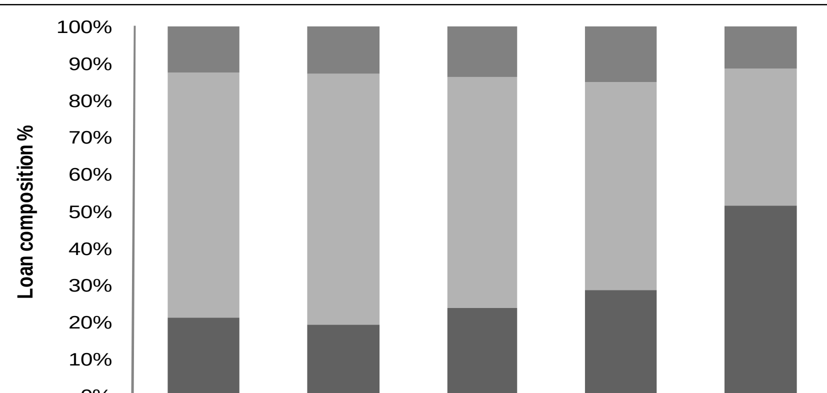

| | FY Mar 2007 | FY Mar 2008 | FY Mar 2009 | FY Mar 2010 | FY Mar 2011 |
|---|---|---|---|---|---|
| Other Assets | 6.85% | 5.69% | 5.87% | 7.82% | 6.55% |
| Net Loans & Advances | 62.36% | 60.75% | 59.21% | 68.27% | 69.60% |
| Real estate | 6.98% | 8.93% | 4.56% | 3.15% | 1.58% |
| Dealing & investment securities | 9.82% | 10.54% | 17.00% | 10.34% | 11.80% |
| Cash & Money At Call | 2.95% | 5.28% | 6.11% | 3.61% | 4.76% |

*Source: Arpico*

***Lease portfolio charted robust growth***

Arpico's credit assets, which constituted 69.60% of its total assets as at end-FY Mar 2011, mainly comprise leasing and HP facilities (refer to Chart 2). The robust loan growth in fiscal 2011 had been driven by the growth of its leasing segment, which had swelled 167.95% to LKR 903.00 million, on the back of the Company's continued concentration on unregistered 3-wheelers and increased sales of passenger cars amid lower import duties.

**Chart 2: Arpico's loan composition**




| | FY Mar 2007 | FY Mar 2008 | FY Mar 2009 | FY Mar 2010 | FY Mar 2011 |
|---|---|---|---|---|---|
| Loans | 12.39% | 12.66% | 13.50% | 15.08% | 11.43% |
| Hire purchase | 66.52% | 67.98% | 62.90% | 56.02% | 37.05% |
| Leases | 21.08% | 19.33% | 23.60% | 28.83% | 51.43% |

*Source: Arpico*

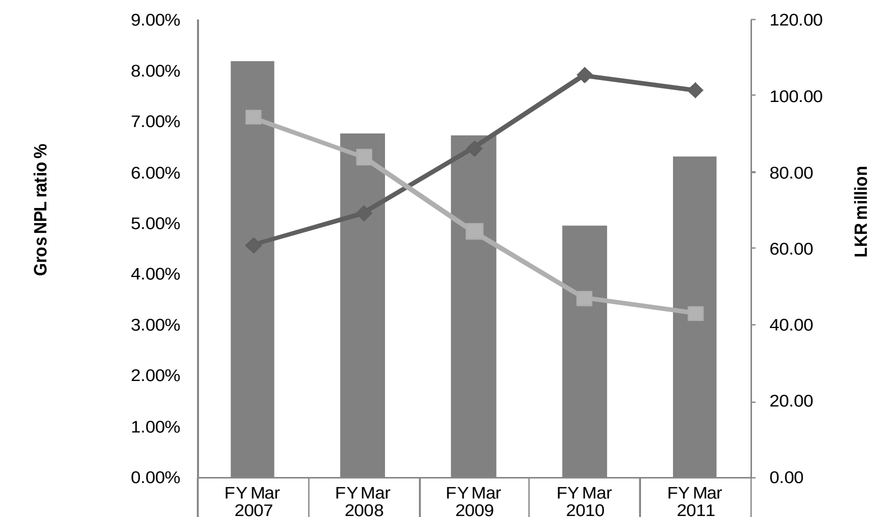
***Concentration on high- yielding segments***

The Company's portfolio concentrates on 3-wheeler financing, currently a high-growth segment with relatively low delinquencies; this accounted for approximately 65% of its lease portfolio. Despite the highly competitive industry, Arpico intends to retain its focus on 3-wheeler financing in light of the rising demand from both and urban and rural areas. Notably, this high-yielding segment had supported Arpico's improved profitability. Moreover, the Company plans to increase its relatively small pawning exposure as this is a high-yielding segment that has relatively low risk because it is fully collateralised with gold.

***Easing gross NPL ratio supported by enlarged loan book***

Amid its robust expansion, the Company's absolute NPLs augmented LKR 18.11 million (or 27.39%) to LKR 84.25 million as at end-FY Mar 2011. Nonetheless, Arpico's gross NPL ratio eased from 3.51% to 3.23% y-o-y. While the improvement is mainly attributable to its loan expansion, its gross NPL ratio was on par with those of its similar rated peers (refer to Chart 3). Although a portion of Arpico's credit assets has yet to be seasoned owing to its robust loan expansion, we expect NPLs to be manageable given the Company's stringent underwriting standards and focus on enlarging 3-wheeler financing and the pawning segment, which have historical low delinquency rates.

**Chart 3: Arpico's gross NPL ratio vs peers'**




| | FY Mar 2007 | FY Mar 2008 | FY Mar 2009 | FY Mar 2010 | FY Mar 2011 |
|---|---|---|---|---|---|
| Gross NPLs - LKR million | 109.28 | 90.26 | 89.69 | 66.14 | 84.25 |
| Gross NPL ratio - industry | 4.56% | 5.19% | 6.46% | 7.90% | 7.60% |
| Gross NPL ratio - Arpico | 7.07% | 6.30% | 4.83% | 3.51% | 3.23% |

*Source: Arpico's annual report, RAM Ratings Lanka*

***Adequate provisioning***

Backed by higher provisioning, the Company's NPL coverage broadened to 56.87% as at end-FY Mar 2011, from 52.19% a year earlier. Arpico's provisioning levels are viewed to be adequate. Consequently, its net NPL ratio eased from 1.71% to 1.42% over same span. Moreover, Arpico's loan-concentration risk remained low, with its top 20 loans accounting for just 3.12% of its entire credit base as at end-FY Mar 2011.

***Discontinuing real-estate business***

Arpico's exposure to real estate has tapered off to just 1.58% of its entire loan base, on the back of the management's decision to discontinue its focus on this segment given the high liquidity risk involved. We note that this segment had hindered the Company's performance in fiscal 2010 due to sluggish demand for real estate. In the short term, Arpico intends to dispose of its remaining land bank and take this segment off its books.

## Performance

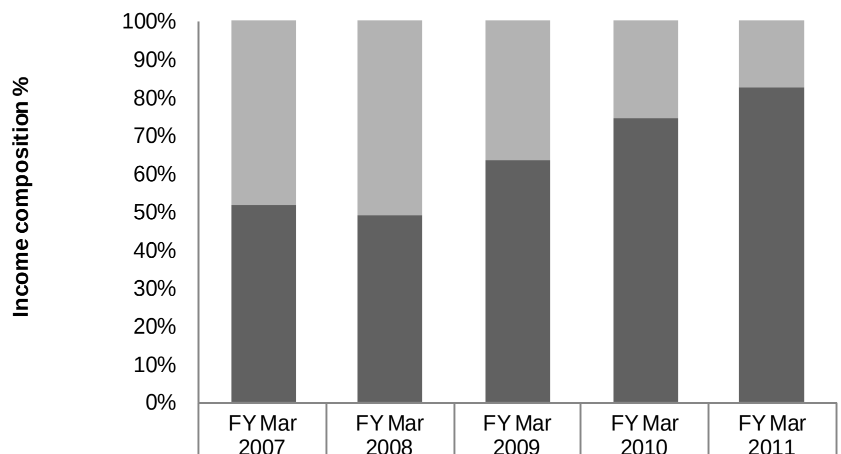
***Improving performance***

Arpico's performance improved in FY Mar 2011, on the back of its robust loan growth that was further supported by its new branch and pawning centres, which had broken even within a year. Meanwhile, the Company's robust loan growth is reflected in its wider margins; its NIM clocked in at 9.68% in FY Mar 2011 (FY Mar 2010: 6.77%). This was also backed by reduced funding costs amid the faster repricing of deposits relative to its fixed-rate HP and leasing facilities in a scenario of tapering interest rates.

***Surge in NII***

Arpico's exceptional profitability in fiscal 2011 was mainly underpinned by the surge in its net interest income ("NII"). Its top line was lifted 22.27% y-o-y to LKR 380.24 million, driven by its enlarged loan base. This, together with lower funding costs amid tapering interest rates, had resulted in a 72.99% y-o-y jump in its NII in FY Mar 2011. As such, the proportion of NII in its gross income came up to 82.40% (refer to Chart 4). Going forward, we expect Arpico's top line to increase steadily, supported by new pawning centres and branches amid the generally more conducive domestic economic landscape.

**Chart 4: Arpico's income composition**



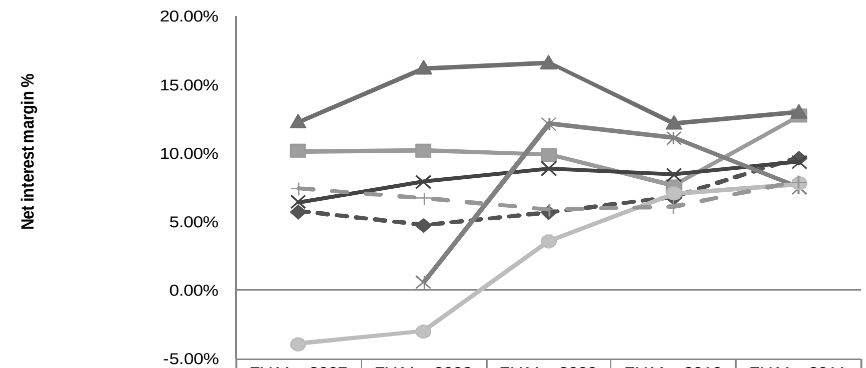

| | FY Mar 2007 | FY Mar 2008 | FY Mar 2009 | FY Mar 2010 | FY Mar 2011 |
|---|---|---|---|---|---|
| Non-interest income | 48.33% | 50.95% | 36.78% | 25.57% | 17.60% |
| Net interest income | 51.67% | 49.05% | 63.22% | 74.43% | 82.40% |

*Source: Arpico*

***Wider NIM***

The surge in Arpico's NII had translated into healthier margins; its NIM widened to 9.68% in FY Mar 2011 compared to 6.77% a year earlier (refer to Chart 5). We note that the broader margin was backed by reduced funding costs, complemented by Arpico's focus on more lucrative 3-wheeler financing facilities and pawn broking, which enjoys robust demand. However, we expect the Company's NIM to be pressured by the downward repricing of its credit assets as funding costs remain unchanged in the short term.

**Chart 5: Arpico's NIM vs peers'**




| | FY Mar 2007 | FY Mar 2008 | FY Mar 2009 | FY Mar 2010 | FY Mar 2011 |
|---|---|---|---|---|---|
| Arpico Finance (BB) | 5.73% | 4.75% | 5.71% | 6.77% | 9.68% |
| Commercial Credit (BB) | 10.13% | 10.18% | 9.85% | 7.62% | 12.69% |
| AMF (BB-) | 12.30% | 16.26% | 16.62% | 12.21% | 13.03% |
| Nanda Investments (BB-) | 6.44% | 7.90% | 8.90% | 8.45% | 9.35% |
| BLI (BB) | | 0.61% | 12.15% | 11.17% | 7.49% |
| Swarnamahal Finance (BB+) | -3.89% | -3.00% | 3.60% | 7.09% | 7.79% |
| Industry average | 7.43% | 6.68% | 5.85% | 6.07% | 7.91% |

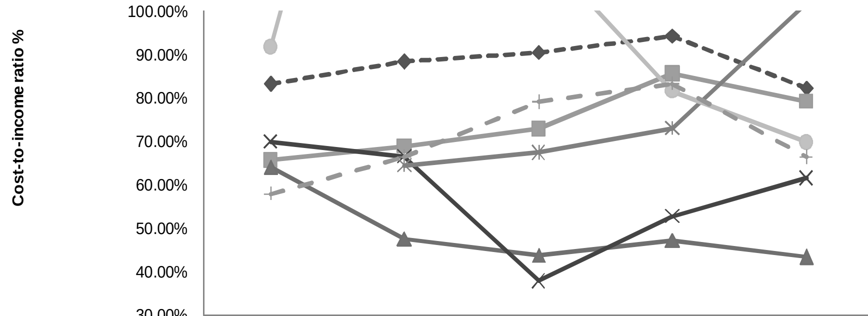
*Source: Arpico annual report*, *RAM Ratings Lanka*

*Commercial Credit = Commercial Credit Limited; AMF: Associated Motor Finance Co Ltd = Nanda Investments = Nanda Investments Ltd; BLI = Bimputh Lanka Investment Limited; Swarnamahal Finance = Swarnamahal Finance Co Ltd*

***Improved cost-to-income ratio, albeit still weak***

Traditionally, Arpico's operational efficiency have been weak, as reflected by its high cost-to-income ratio relative to its similar rated peers' (refer to Chart 6); this is because most of its operations had been undertaken manually. Despite the 36.14% y-o-y climb in operating expenses, the Company's cost-to-income ratio had been trimmed on the back of higher revenue that was supported by its newly opened branch and the pawning centres reaching break-even levels. As such, its cost-to-income ratio had eased to 82.21% during the review period from 94.36% in the previous year. Nevertheless, we expect the Company's overheads to increase in line with its anticipated branch expansion; this may suppress its bottom-line growth until the new branches break even.

**Chart 6: Arpico's cost-to-income ratio vs peers**




| | FY Mar 2007 | FY Mar 2008 | FY Mar 2009 | FY Mar 2010 | FY Mar 2011 |
|---|---|---|---|---|---|
| Arpico Finance (BB) | 83.12% | 88.21% | 90.48% | 94.35% | 82.21% |
| Commercial Credit (BB) | 65.60% | 68.90% | 72.72% | 85.50% | 79.16% |
| AMF (BB-) | 63.99% | 47.61% | 43.74% | 47.24% | 43.16% |
| Nanda Investments (BB-) | 69.75% | 66.34% | 37.73% | 52.75% | 61.38% |
| BLI (BB) | | 64.26% | 67.28% | 72.85% | 101.66% |
| Swarnamahal Finance (BB+) | 91.72% | 203.65% | 114.65% | 81.50% | 69.67% |
| Industry average | 57.85% | 66.45% | 78.93% | 83.35% | 66.29% |

*Source: Arpico annual report, RAM Ratings Lanka*

***Share-trading gains offset lower real-estate income***

In terms of non-interest income, we note that its share had been trimmed to 17.60% as Arpico wound down its real-estate business, which had previously been a significant contributor (FY Mar 2010: 25.57%). The turnaround of the gross income mix was underpinned by the growing prominence of interest income on the back of its loan expansion. However, the weaker income from its real-estate business had been partially offset by share-trading gains amid the buoyant stock market.

***Better ROA***

The Company's enlarged gross income had shored up its profitability, leading to a pre-tax profit of LKR 36.20 million in FY Mar 2011. As such, Arpico recorded a return on assets ("ROA") of 2.00% at the end of the period (end-FY Mar 2010: 0.62%); this was at par with those of its similar-rated peers.

***Anticipated uptick in performance***

Moving ahead, RAM Ratings Lanka expects Arpico to maintain its growth momentum over the medium term. Nevertheless, we envisage the Company's overheads to rise in line with its anticipated branch expansion; this may suppress its bottom-line growth until the new branches break even. Furthermore, we believe that Arpico's performance will be supported by its steady growth in loan book and healthy asset quality.

## Funding & Liquidity

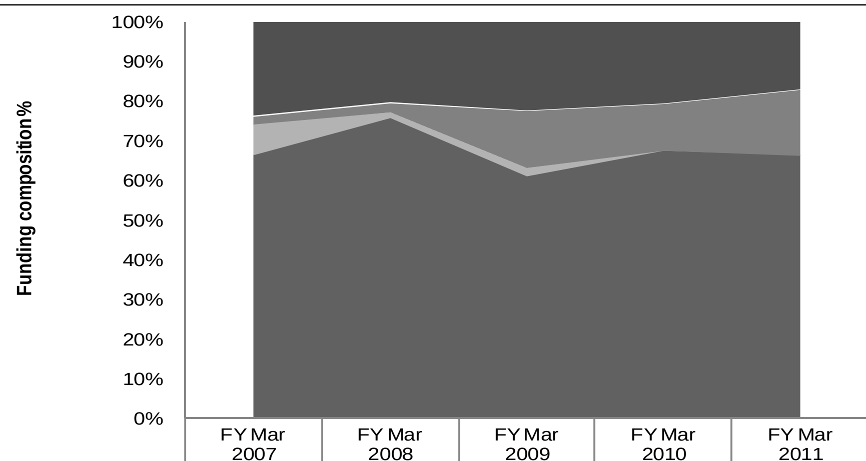
***Moderate funding and liquidity positions***

RAM Ratings Lanka opines that Arpico has adequate funding and liquidity levels. Its funding base has been dominated by deposits, further supported by increased long-term borrowings. Nonetheless, the Company's liquidity position had diminished as a result of channelling its funds to rapidly expand its loan book, as mirrored by its declined statutory liquid-asset ratio of 12.87% as at end-FY Mar 2011 (end-FY Mar 2010: 18.20%).

***Deposits – Chief funding source***

Arpico's funding mix is dominated by deposits. Public deposits fulfilled 66.33% of the Company's funding needs in fiscal 2011 while borrowings and shareholders' funds accounted for a respective 16.49% and 17.19% (refer to Chart 7). At the same time, Arpico's deposit base augmented 24.75% y-o-y, aided by its new branch and strong brand name. Meanwhile, Arpico's deposit concentration had eased as at end-FY Mar 2011, with its top 20 depositors accounting for 12.54% of its total deposits.

**Chart 7: Arpico's funding composition**




| | FY Mar 2007 | FY Mar 2008 | FY Mar 2009 | FY Mar 2010 | FY Mar 2011 |
|---|---|---|---|---|---|
| Shareholders' funds | 23.83% | 20.45% | 22.53% | 20.76% | 17.19% |
| Long-term borrowings | 1.94% | 2.37% | 14.31% | 11.60% | 16.49% |
| Short-term borrowings | 7.79% | 1.40% | 2.12% | 0.19% | 0.00% |
| Customer deposits | 66.44% | 75.79% | 61.04% | 67.46% | 66.33% |

*Source: Arpico*

***Increased reliance on borrowings***

We note that the Company had relied on borrowings to fuel its robust 26.19% loan growth in FY Mar 2011. As such, Arpico's debt level had leapt 80.37% y-o-y. It had mainly obtained funds from banks by pledging its leasing and HP receivables to its financiers; these borrowings that tilt towards the long term are viewed positively as they allow better matching of asset-liability maturities. In line with the accretion of its credit assets, Arpico's LD ratio weakened to 112.61% as at end-FY Mar 2011 (end-FY Mar 2010: 108.77%), albeit still better than those of its similar-rated peers.

***Easing maturity mismatches***

Nonetheless, we note that the 1-year gap in the Company's asset-liability maturity mismatch had eased on the back of its reliance on long-term borrowings. As such, the negative gap of 82.12% for total interest-earning assets in the "less than 3 months" bucket in FY Mar 2010 had improved to negative 55.52% by end-FY Mar 2011 (refer to Table 1). Arpico partially mitigates the short-term maturity mismatches via the expansion of its pawning advances and small-ticket loans, which typically have shorter tenures. Besides, we derive some comfort from its healthy deposit-renewal rate of more than 90%. However, Arpico does not have much in the way of funding lines, which amount to only LKR 50 million.

**Table 1: Arpico's maturity mismatches**

| | As at end-Mar 2010 | | | As at end-Mar 2011 | | |
|---|---|---|---|---|---|---|
| | <1 year | 1 to 3 years | >3 years | <1 year | 1 to 3 years | >3 years |
| Interest earning assets | 547.62 | 451.72 | 226.22 | 845.83 | 470.79 | 327.07 |
| Interest bearing liabilities | 997.33 | 145.15 | 36.10 | 1,315.48 | 219.40 | 27.96 |
| Gap | (449.71) | 306.58 | 190.12 | (469.65) | 251.39 | 299.11 |
| **Cumulative gap** | **(449.71)** | **(143.13)** | **46.98** | **(469.65)** | **(218.26)** | **80.86** |
| % of interest earning assets | -82.12% | -31.69% | 20.77% | -55.52% | -46.36% | 24.72% |

*Source: Arpico*

## Capital Adequacy

***Adequate capital cushioning***

Arpico's capital cushioning is deemed adequate. Despite the expansion of its credit assets, its tier-1 and overall RWCARs clocked in at 13.91% and 16.06%, respectively, as at end-FY Mar 2011 (end-FY Mar 2010: 14.83% and 17.51%). Although we expect the Company's capital cushioning to moderate in line with the anticipated expansion of its loan books, we still expect it to be comfortable. Notably, Arpico is required to increase its capital base to LKR 300 million by end-December 2013, from LKR 235.69 million as at end-FY Mar 2011, in accordance with the CBSL's regulations, which the Company intends to meet via internal capital. Given its commendable asset quality and prudent provisioning, the Company's ratio on net NPLs to shareholders' funds was kept at a low 6.16% as at end-FY Mar 2011 (end-FY Mar 2010: 6.04%).

## Corporate Information – Arpico Finance Company PLC

**Date of Incorporation:** 1951

**Commencement of Business:** 1951

**Major Shareholders (as at end-March 2011):**

| | |
|---|---|
| Alfinco Insurance Brokers (Pvt) Ltd | 40.56% |
| Alliance Finance Company Ltd | 19.54% |
| Mr KDD Perera | 6.67% |
| Mr JR de Silva | 2.22% |
| Mr RKEP de Silva | 1.99 % |
| Mr S Abishek | 1.86 % |
| Orient Hotels Ltd | 1.85 % |
| Mr OD Liyanage | 1.58 % |
| Mr MAH Esufally | 1.50% |

**Directors:**

| | |
|---|---|
| Mr Pratapkumar De Silva | Chairman |
| Mr DLSR Perera | |
| Mr Senakke Bandaranayake | |
| Ms Ruvini Weerasinghe | |
| Mr Bede Jayalath | |
| Mr Romani De Silva | |
| Mr Lyle Denise Peiris | |

**Auditor:**

M/s SJMS Associates (External Auditors)
M/s HLB Edirisinghe & Co. (Internal Auditors)

**Listing:** Listed on the Colombo Stock Exchange

**Key Management:**

| | |
|---|---|
| Mr Senakke Bandaranayake | Joint Managing Director |
| Mr Bede Jayalath | Director – Finance |
| Ms Ruvini Weerasinghe | Director – Legal |
| Mr Dharshan Silva | Chief Operating Officer |

**Major Subsidiaries:**

**Capital History:**

| Year | Remarks | Amount (LKR million) | Cumulative Total (LKR million) |
|---|---|---|---|
| 1951 | First allotment | 0.38 | 0.38 |
| 1972 | New ordinary share issue | 0.38 | 0.76 |
| 1989 | New ordinary share issue | 3.75 | 4.50 |
| 1993 | New ordinary share issue | 6.00 | 10.50 |
| 1994 | New ordinary share issue | 5.25 | 15.75 |
| 1951 | Redeemable preference share issue | 0.13 | 15.88 |
| 1958 | Irredeemable preference share issue | 0.50 | 16.38 |
| 1971 | Redemption of redeemable preference shares | (0.13) | 16.25 |
| 2008 | Rights issue | 14.44 | 30.69 |
| 2009 | Rights issue | 65.62 | 96.31 |

# FINANCIAL SUMMARY
## Arpico Finance Company PLC – Company

| BALANCE SHEET (LKR Million) | 31-Mar-07 | 31-Mar-08 | 31-Mar-09 | 31-Mar-10 | 31-Mar-11 |
|---|---|---|---|---|---|
| ASSETS | | | | | |
| Cash & Money At Call | 0.62 | 29.14 | 34.52 | 47.65 | 46.39 |
| Deposits & Placements With Financial Institutions | 25.16 | 28.37 | 50.67 | 10.00 | 50.00 |
| Securities Purchased Under Resale Agreements | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Securities | | | | | |
| Dealing Securities | 22.06 | 1.90 | 11.35 | 6.84 | 6.98 |
| Investment Securities | 63.86 | 111.00 | 222.46 | 152.98 | 221.68 |
| Gross Loans & Advances | 643.58 | 731.06 | 895.23 | 1,167.99 | 1,502.59 |
| Interest-In-Suspense | 68.61 | 47.20 | 48.77 | 56.23 | 66.65 |
| General Loan Loss Reserves | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Specific Loan Loss Reserves | 29.13 | 21.74 | 21.02 | 20.37 | 26.34 |
| Net Loans & Advances | 545.84 | 662.13 | 825.45 | 1,091.38 | 1,409.60 |
| Investments in Subsidiaries/Associates | 0.00 | 1.93 | 3.24 | 5.44 | 10.29 |
| Investment Land and Properties | 61.10 | 97.38 | 63.51 | 50.37 | 32.02 |
| Other Assets | 59.97 | 62.05 | 81.88 | 124.96 | 132.68 |
| Property, Plant and Equipment | 96.64 | 96.01 | 100.97 | 109.08 | 115.78 |
| TOTAL ASSETS | 875.24 | 1,089.91 | 1,394.06 | 1,598.70 | 2,025.42 |
| LIABILITIES | | | | | |
| Customer Deposits | | | | | |
| Savings | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Fixed | 541.86 | 767.47 | 796.13 | 1,003.34 | 1,251.71 |
| 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 Agreements | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Other Borrowing | 79.34 | 38.12 | 214.27 | 175.28 | 311.13 |
| Subordinated Debt & Hybrid Capital | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Other Liabilities | 59.70 | 77.23 | 89.87 | 111.30 | 138.24 |
| TOTAL LIABILITIES | 680.89 | 882.82 | 1,100.27 | 1,289.92 | 1,701.08 |
| Paid-up Capital | 16.25 | 16.25 | 96.31 | 96.31 | 96.31 |
| Minority Interest | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Share Premium & Other Reserves | 97.32 | 97.32 | 97.32 | 107.32 | 102.32 |
| Statutory General Reserve | 22.62 | 25.62 | 28.06 | 30.41 | 35.42 |
| Retained Profits/(Loss) | 58.16 | 67.89 | 72.09 | 74.74 | 90.29 |
| Total Shareholders' Funds | 194.35 | 207.09 | 293.78 | 308.78 | 324.34 |
| TOTAL LIABILITIES & SHAREHOLDERS' FUNDS | 875.24 | 1,089.91 | 1,394.05 | 1,598.70 | 2,025.42 |
| | | | | | |
| COMMITMENTS & CONTINGENCIES | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| TIER 1 CAPITAL | 78.90 | 75.14 | 204.38 | 209.81 | 235.69 |
| CAPITAL BASE | 113.17 | 109.41 | 245.72 | 247.81 | 272.16 |

# FINANCIAL SUMMARY
## Arpico Finance Company PLC – Company

| INCOME STATEMENT (LKR Million) | 31-Mar-07 | 31-Mar-08 | 31-Mar-09 | 31-Mar-10 | 31-Mar-11 |
|---|---|---|---|---|---|
| Interest Income | 125.60 | 168.68 | 262.30 | 310.98 | 380.24 |
| 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 | 79.89 | 122.02 | 191.45 | 209.61 | 204.88 |
| Net Interest Income | 45.71 | 46.66 | 70.86 | 101.37 | 175.36 |
| Non-Interest Income | 42.76 | 48.47 | 41.22 | 34.82 | 37.44 |
| Gross Income | 88.46 | 95.13 | 112.07 | 136.19 | 212.81 |
| Personnel Expenses | 31.22 | 34.99 | 41.88 | 54.29 | 80.82 |
| Other Non-Interest Expenses | 42.31 | 48.92 | 59.52 | 74.21 | 94.13 |
| Loan Loss Provisions | (6.00) | (8.28) | (3.91) | 1.03 | 6.86 |
| Share of results of Associated Companies | 0.00 | 0.64 | 0.98 | 2.64 | 5.20 |
| Pre-Tax Profit | 20.93 | 20.14 | 15.56 | 9.30 | 36.20 |
| Taxation | 4.63 | 5.12 | 3.37 | (2.42) | 11.13 |
| Profit After Tax | 16.31 | 15.02 | 12.19 | 11.72 | 25.07 |
| Extraordinary Items | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Prior Year Adjustments | 44.51 | 1.69 | 0.00 | 0.00 | 0.00 |
| Minority Interests | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Transfer To Statutory Reserves | 3.26 | 3.00 | 2.44 | 2.34 | 0.00 |
| Transfer To Other Reserves | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Dividend | 4.77 | 3.98 | 5.55 | 6.73 | 0.00 |
| Retained Profit For The Year | 52.79 | 9.73 | 4.20 | 2.65 | 25.07 |

# FINANCIAL RATIOS
## Arpico Finance Company PLC – Company

| KEY RATIOS (%) | 31-Mar-07 | 31-Mar-08 | 31-Mar-09 | 31-Mar-10 | 31-Mar-11 |
|---|---|---|---|---|---|
| Profitability | | | | | |
| Net Interest Margin | 5.73% | 4.75% | 5.71% | 6.77% | 9.68% |
| Non-Interest Income Margin | 5.36% | 4.93% | 3.32% | 2.33% | 2.07% |
| Cost To Income | 83.12% | 88.21% | 90.48% | 94.35% | 82.21% |
| Return On Assets | 2.62% | 2.05% | 1.25% | 0.62% | 2.00% |
| Return On Equity | 12.58% | 10.03% | 6.21% | 3.09% | 11.44% |
| Dividend Payout | 29.22% | 26.48% | 45.56% | 57.43% | 0.00% |
| Asset Quality | | | | | |
| Gross NPL Ratio | 7.07% | 6.30% | 4.83% | 3.51% | 3.23% |
| Net NPL Ratio | 2.12% | 3.22% | 2.41% | 1.71% | 1.42% |
| Specific Loan Loss Provisions For Current Year | 0.96% | 1.26% | 1.47% | 0.73% | 1.07% |
| Gross NPL Coverage | 71.61% | 50.48% | 51.36% | 52.19% | 56.87% |
| Loan Loss Reserve Coverage | 5.07% | 3.18% | 2.48% | 1.83% | 1.83% |
| Liquidity & Funding | | | | | |
| Liquid Asset Ratio | 18.45% | 21.80% | 38.72% | 21.61% | 22.77% |
| Statutory Liquid Asset Ratio | 15.86% | 18.91% | 32.72% | 18.20% | 20.02% |
| Customer Deposits To Total Interest Bearing Funds | 87.23% | 95.27% | 78.79% | 85.13% | 80.09% |
| Loans To Deposits Ratio | 100.74% | 86.27% | 103.68% | 108.77% | 112.61% |
| Loans To Stable Funds Ratio | 75.93% | 72.38% | 68.79% | 79.50% | 80.04% |
| Capital Adequacy | | | | | |
| Shareholders' Funds To Total Assets | 22.21% | 19.00% | 21.07% | 19.31% | 16.01% |
| Tier 1 Risk Weighted Capital Adequacy Ratio | 10.81% | 8.59% | 19.10% | 14.83% | 13.91% |
| Overall Risk Weighted Capital Adequacy Ratio | 15.51% | 12.50% | 22.97% | 17.51% | 16.06% |
| Internal Rate Of Capital Generation | 6.94% | 5.50% | 2.65% | 1.66% | 7.92% |

Note :

* annualised

NA = Not available / Not applicable

# CREDIT RATING DEFINITIONS

## Financial Institution Ratings

A Financial Institution Rating ("FIR") is RAM Ratings Lanka's current opinion on the overall capacity of a financial institution to meet its financial obligations. The opinion is not specific to any particular financial obligation, as it does not take in to account the expressed terms and conditions of any specific financial obligation.

### Long-Term Ratings

| | |
|---|---|
| **AAA** | A financial institution rated AAA has a superior capacity to meet its financial obligations. This is the highest long-term FIR assigned by RAM Ratings Lanka. |
| **AA** | A financial institution rated AA has a strong capacity to meet its financial obligations. The financial institution is resilient against adverse changes in circumstances, economic conditions and/or operating environments. |
| **A** | A financial institution rated A has an adequate capacity to meet its financial obligations. The financial institution is more susceptible to adverse changes in circumstances, economic conditions and/or operating environments than those in higher-rated categories. |
| **BBB** | A financial institution rated BBB has a moderate capacity to meet its financial obligations. The financial institution is more likely to be weakened by adverse changes in circumstances, economic conditions and/or operating environments than those in higher-rated categories. This is the lowest investment-grade category. |
| **BB** | A financial institution rated BB has a weak capacity to meet its financial obligations. The financial institution is highly vulnerable to adverse changes in circumstances, economic conditions and/or operating environments. |
| **B** | A financial institution rated B has a very weak capacity to meet its financial obligations. The financial institution has a limited ability to withstand adverse changes in circumstances, economic conditions and/or operating environments. |
| **C** | A financial institution rated C has a high likelihood of defaulting on its financial obligations. The financial institution is highly dependent on favourable changes in circumstances, economic conditions and/or operating environments, the lack of which would likely result in it defaulting on its financial obligations. |
| **D** | A financial institution rated D is currently in default on either all or a substantial portion of its financial obligations, whether or not formally declared. The D rating may also reflect the filing of bankruptcy and/or other actions pertaining to the financial institution that could jeopardise the payment of the financial obligations. |

### Short-Term Ratings

| | |
|---|---|
| **P1** | A financial institution rated P1 has a strong capacity to meet its short-term financial obligations. This is the highest short-term FIR assigned by RAM Ratings Lanka. |
| **P2** | A financial institution rated P2 has an adequate capacity to meet its short-term financial obligations. The financial institution is more susceptible to the effect of deteriorating circumstances than those in the highest-rated category. |
| **P3** | A financial institution rated P3 has a moderate capacity to meet its short-term financial obligations. The financial institution is more likely to be weakened by the effects of deteriorating circumstances than those in the higher-rated category. This is the lowest investment-grade category. |
| **NP** | A financial institution rated NP has a doubtful capacity to meet its short-term financial obligations. The financial institution faces major uncertainties that could compromise its capacity for payment of financial obligations. |
| **D** | A financial institution rated D is currently in default on either all or he D rating may also reflect the filing of bankruptcy and/or other actions pertaining to the financial institution that could jeopardise the payment of the financial obligations. |

*For long-term ratings, RAM Ratings Lanka applies signs plus (+), flat or minus (-) in each category from AA to C. The sign plus (+) indicates that the financial institution ranks at the higher end of its generic rating category; the sign flat indicates a mid-ranking; and the sign minus (-) indicates that the financial institution ranks at the lower end of its generic rating category.*

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