



RATINGS

## Media Release

### **RAM Ratings Lanka reaffirms The Multi Finance Limited's ratings**

RAM Ratings Lanka has reaffirmed the long- and short-term ratings of The Multi Finance Company Limited ("MFL" or "the Company") of BB- (with a stable outlook) and NP, respectively. The ratings are premised on the Company's small size and concentration risks arising from exposure to large loans. These factors are, nonetheless, moderated by the fact that MFL has met the minimum core-capital requirement of LKR 200 million, which has consequently improved the Company's capital adequacy and liquidity levels.

MFL remains one of the smallest players in the registered finance companies ("RFCs") industry, accounting for 0.19% of the industry asset base as at end-December 2008. Meanwhile, the Company complied with the regulatory minimum core capital requirement (of LKR 200 million) mainly through the investment by Entrust Limited ("Entrust"), formerly Ceylinco Shriram Securities Holdings Limited. Entrust now has a 92.13% stake in the Company. Consequently, certain key functions were taken over by the new management team. The new management line-up is focused on streamlining MFL's back-office operations and tightening collections as well as recoveries. In this regard, all manual systems are being automated; this is envisaged to facilitate efficient monitoring and control.

Furthermore, under the new management, the Company has expanded its branch network; opening 2 branches in Matara and Kurunegala in the space of two months. This expansion may exacerbate the Company's operational risks and potentially transform its credit profile; as such, the new team's risk-management capabilities will be vital. Over the long term, the new management will have a bearing on the Company's asset quality. Improved recoveries and monitoring helped rein in NPLs from LKR 6.65 million as at end-FY Mar 2008 to LKR 4.25 million as at end-December 2008.

However, our concerns lie in the large loan exposures and the unseasoned loan portfolio. MFL's top 10 loans accounted for 27.14% of gross loans as at end-December 2008, even a few defaults on these loans could significantly deteriorate the Company's asset quality. Moreover, recovery efforts, with respect to mortgage-backed loans, could be hindered as the Company does not have *parate*<sup>1</sup> execution rights. As the Company begins to expand its portfolio, however, concentration risk is expected to be diluted, albeit still significant. Going forward, the management of MFL will limit their exposure in mortgage loans to 50% of the land value, and will extend these loans only on bare lands. The Company's loan book expanded from LKR 57.39 million to LKR 125.63 million during the first 9 months of FY Mar 2009. Although we note that the Company has adopted more stringent credit evaluation procedures, the long-term health of the loan portfolio will come to light once it seasons. This will inturn determine Company's financial performance in the long run.

The financial performance of MFL remained weighed down by rising interest expenses and heavy overheads. MFL's pre-tax profit has shrunk from LKR 5.95 million as at end-FY Mar 2006 to LKR 2.90 million as at end-FY Mar 2008. The Company's cost-to-income ratio of 85.40% as at end-FY Mar 2008 was weaker than the industry average of 66.45% as at the same date. Although MFL's short-term performance may improve owing to the correction in its policy on interest-income recognition (as per SLAS 33), its long-term performance still depends on the health of its loan portfolio.

---

<sup>1</sup> Rights generally given to state-owned and some commercial banks, to seize and dispose of property without legal proceedings.

Following the capital injection by Entrust, MFL now excess liquidity; its statutory liquid-asset ratio stood at 172.70% as at end-December 2008 (end-May 2009: 45.46%). In addition, its Tier-1 risk-weighted capital-adequacy ratio ("RWCAR") and overall RWCAR clocked in at 103.90% and 113.30%, respectively - well above the corresponding regulatory minimums of 5% and 10%. However, the Company's internal capital generation (end-March 2008: 1.70%; end-December 2008: 0.56%) remained poorer than the industry average (end-December 2008: 8.74%) due to its weak financials. Although RAM Ratings Lanka expects MFL's capital adequacy to return to industry levels over the medium term, the Company's long-term adequacy would still be dictated by its asset quality and, in turn, its internal capital generation.

**Analyst Contact**

Prakash Jerome  
prakash@ram.com.lk