


RATINGS

CREDIT RATING RATIONALE

FINANCIAL INSTITUTIONS – SRI LANKA
A wholly owned subsidiary of RAM Holdings Berhad

MERCHANT BANK OF SRI LANKA PLC – Rating Review

Financial Institution
Ratings:

Long-term: AA- [Reaffirmed]

Short-term: P1 [Reaffirmed]

Rating Outlook:

Stable

Instruments:

 (i) LKR 300 million unsecured
unlisted private
debentures (2007/2010)

 (ii) LKR 500 million unsecured
unlisted public debentures

Ratings:

(i) AA- [Reaffirmed]

(ii) AA- [Reaffirmed]

Coupon Rates:

 (i) Weighted-average 1-year
Treasury bill rate,
excluding withholding tax
+ 300 basis points, with
a cap of 17% and a floor
of 13%.

 (ii) Type A: 3-year fixed rate
of 16.5%, payable semi-
annually.

 Type B: 4-year fixed rate
of 16.5%, payable semi-
annually.

 Type C: 3-year floating
rate of 6-month Treasury
bill + 1.5%, payable
semi-annually.

 Type D: 4-year floating
rate of 6-month Treasury
bill + 1.5%, payable
semi-annually.

Strengths:

- Sovereign-owned parent
- Adequate capital

Weaknesses:

- Weak asset quality
- Funding commitment to
subsidiaries

Summary

RAM Ratings Lanka has reaffirmed Merchant Bank of Sri Lanka's ("MBSL" or "the Company") long- and short-term financial institution ratings at AA- and P1, respectively. At the same time, the AA- ratings of the Company's LKR 300 million Unlisted Private Debentures and LKR 500 million Unlisted Public Debentures have also been reaffirmed. All the long-term ratings have a stable outlook. The ratings are premised on the financial flexibility derived from the Company's parent, the sovereign-owned Bank of Ceylon ("BOC").

MBSL is a 72.14%-owned subsidiary of BOC, i.e. Sri Lanka's largest licensed commercial bank ("LCB") in terms of assets; BOC accounted for 21.50% of the LCB industry's assets as at end-December 2009. On the other hand, MBSL remains a small player in the market, accounting for only 4.99% of the specialised leasing industry's ("SLC") asset base as at the same date. Despite its small size, MBSL's ratings remain supported by solid parental backing. BOC has consistently demonstrated its support to MBSL via equity injections and loans; in December 2009, it infused LKR 347.91 million into the Company by way of a rights issue.

On a separate note, MBSL acquired a specialised savings bank (rebranded as MBSL Savings Bank Ltd or "MBSL Savings") and an insurance company (rebranded as MBSL Insurance) in 2009; these companies had been experiencing financial difficulties amid the domestic financial turmoil. We note that the turnaround of these entities has not been as rapid as anticipated. That said, these subsidiaries had been acquired at a relative bargain, with a total investment value of LKR 238.61 million (or 10.23% of its capital) that translates into 4.28% of the Company's total assets as at end-December 2009.

Meanwhile, the Company's asset quality has remained weaker than the overall industry's - albeit having taken a turn for the better during the reviewed period. MBSL's gross non-performing-loan ("NPL") ratio ameliorated to 10.47% as at end-FY Dec 2009, from 12.46% a year earlier; the ratio had eased further to 10.16% by end-March 2010. The improvement had been primarily driven by recoveries and loan write-offs.

Despite the write-offs, the Company's performance had stayed relatively unchanged during the reviewed period - supported by non-recurring capital gains (LKR 46.73 million) on the disposal of an investment property and also gains from its equity portfolio. Under the circumstances, MBSL's net profit came up to LKR 200.98 million in FYE 31 December 2009 ("FY Dec 2009") (FY Dec 2008: LKR 205.08 million).

Principal Activities:
Provision of leasing,
trade-financing and
other merchant
banking activities

Analysts:

Christy Sugirtharatnam
ACMA
(9411) 2553089
christy@ram.com.lk

Prashani Illangasekera
MSc, BA
(9411) 2553089
prashani@ram.com.lk

Company Contact:
Adrian Perera
MBA, FCMA, FCCA,
FSCMA, AIB
Chief Executive
Officer
(9411) 2596099
adrian@ram.com.lk

Website:
www.ram.com.lk

*First Merchant
Bank in Sri Lanka*

*Acquisition of
subsidiaries &
managing of
financially weak
firms*

Meanwhile, the Company's shareholders' funds still dominate its funding structure, accounting for 46.03% of total funding following its rights issue in FY Dec 2009. Concurrently, MBSL has substituted short-term borrowings for long-term debts, to benefit from the environment of receding interest rates. However, the envisaged improvement has not materialised due to its heftier borrowings. Going forward, we are concerned about the funding commitments that MBSL may have with regard to its recently acquired subsidiaries. In addition to the LKR 1.43 billion shortfall vis-à-vis meeting the minimum capital requirement for MBSL Savings by December 2012 and the LKR 62.46 million needed by MBSL Insurance, the Company may also have to infuse additional capital to sustain its newly acquired subsidiaries.

That said, we note that MBSL's gearing ratio of 1.18 times as at end-FY Dec 2009 is well below the regulatory cap of 7 times, thus allowing much room for further leverage. Meanwhile, we opine that the Company is adequately capitalised, with LKR 2.33 billion of shareholders' funds as at the same date.

Outlook

The stable outlook on MBSL's long-term ratings reflects the steadfast financial support of BOC and the resultant financial flexibility. Downward rating pressure may be exerted if the Company's asset quality deteriorates significantly; the easing of financial support from its parent will also have negative rating implications. Under the present circumstances, upward revision of the ratings is unlikely over the medium term.

Corporate Profile

In response to a request by the World Bank, BOC had initially established MBSL as its management-consultancy division in 1980, to cater to the advisory needs of the corporate sector. MBSL which was Sri Lanka's first Merchant Bank, was later incorporated as a public limited company and was subsequently listed on the Colombo Stock Exchange in 1991.

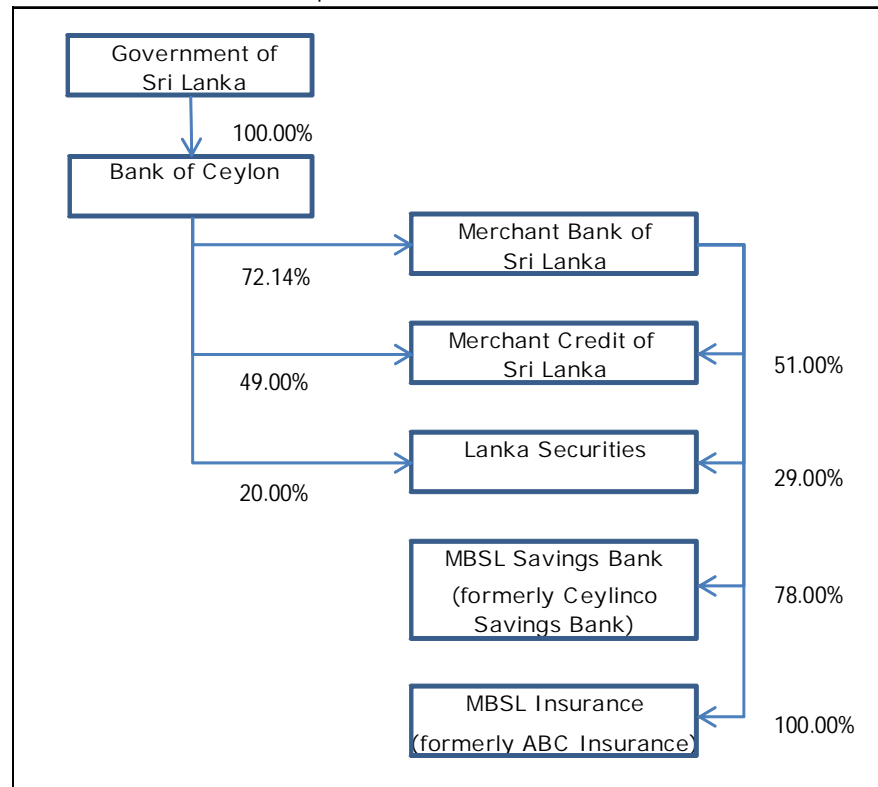
MBSL falls under the regulatory purview of the Central Bank of Sri Lanka ("Central Bank") as a registered finance-leasing establishment, under the Finance Leasing Act No. 56 of 2000. MBSL is also registered under the Securities and Exchange Commission ("SEC") Act No. 36 of 1987 - as an investment manager, margin provider and underwriter.

Following the collapse of several Ceylinco-related financial institutions in the early part of 2009, MBSL had had the opportunity to secure a much-sought-after specialised banking licence. As such, MBSL had acquired Ceylinco Savings Bank ("CSB"), which has now been rebranded as MBSL Savings Bank; the latter is primarily involved in accepting public deposits, leasing, hire-purchase ("HP") and provision of loans. In April 2009, MBSL acquired the troubled ABC Insurance Company (which has been rebranded as MBSL Insurance), with the objective of venturing into the insurance industry. Meanwhile, the Company had also been appointed as a managing agent for several troubled Ceylinco financial institutions, including The Finance PLC, i.e. Sri Lanka's largest registered finance company ("RFC"). MBSL currently holds a 15%-stake in The Finance PLC; this may increase to approximately 37% during the course of this year.

Continuing stakes in Associate & Subsidiary

In addition to its recently acquired subsidiaries, MBSL also owns 51% of Merchant Credit Sri Lanka (“MCSL”), an RFC; the other 49% is held by BOC (refer to Chart 1). MCSL is engaged in leasing, HP, loans, real estate and acceptance of public deposits. MCSL’s asset base amounted to LKR 3.82 billion as at end-FY Dec 2009. Elsewhere, MBSL holds an associate stake of 29% in Lanka Securities Limited (“LSL”), a registered stockbroker. BOC and First Capital Securities Corporation Limited of Pakistan own another 20% and 51%, respectively. LSL’s asset base amounted to LKR 504.49 million as at end-FY Dec 2009; it recorded a pre-tax profit of LKR 100.37 million last year.

Chart 1: MBSL’s ownership structure



Ownership

MBSL’s rating remains anchored by the strength of its sovereign-owned parent. BOC is Sri Lanka’s largest commercial bank, with an asset base of LKR 537.24 billion as at end-FY Dec 2009, accounting for 23.82% of the LCB industry’s assets as at the same date. BOC has consistently demonstrated its financial support for MBSL; after a capital reorganisation, the parent subscribed for a 1:2 rights issue in 2005. In 2009, BOC subscribed to MBSL’s rights issue, thereby injecting a further LKR 347.91 million.

Management & Strategies

In line with the appointment of new officials to state institutions after the country’s general elections in April 2010, Mr M R Shah has been appointed the Chairman of MBSL. He is a banker by profession, with 33 years of experience in the sector; he had also headed the Ceylon Bankers Employees’ Union (or CBEU) for 10 years. The Company’s senior management team continues to be led by Mr Gamini Karunathilake, the Chief Executive Officer.

Sovereign owned parent anchors ratings

Appointment of new Chairman

Fragile subsidiaries

RAM Ratings Lanka's concerns hinge on the fragile nature of the Company's recently acquired subsidiaries, which had been purchased under the stewardship of the previous Chairman. The accumulated losses of MBSL Savings had eroded its capital to LKR 66.47 million as at end-FY Dec 2009, significantly below the regulatory minimum requirement of LKR 1.5 billion. This had led to a "going concern" qualification by the auditors. However, the Central Bank had given an extension until December 2012 with regard to the minimum capital requirement. Moreover, RAM Ratings Lanka notes that MBSL Savings had failed to meet the Central Bank's liquidity requirements in FY Dec 2009. On a positive note, MBSL Savings recorded LKR 40.26 million pre-tax profits in FY Dec 2009, after a LKR 371.87 million loss in FY Dec 2008.

Going forward, the management intends to raise approximately LKR 450 million to strengthen MBSL Savings' capital via a share issue in June 2010. Moreover, the Company is currently in the process of selling 10% of MBSL Savings to a foreign investor. The Company also plans to raise additional funds through a rights issue and a listing exercise in December 2010. RAM Ratings Lanka will continue monitoring the developments in this regard.

MBSL Insurance – persistent losses, capital below regulatory minimum

Meanwhile, the turnaround of MBSL Insurance has not been as rapid as anticipated. The Company continued to incur losses in FY Dec 2009 due to its weak competitive position and hefty overheads. Its capital amounted to LKR 137.54 million as at end-FY Dec 2009, below the regulatory minimum of LKR 200 million. However, we note that regulatory pressure has not yet been exerted. Moreover, MBSL Insurance incurred a loss of LKR 66.35 million in FY Dec 2009 following a LKR 86.16 million loss in FY Dec 2008.

Leeway for gearing provides financial flexibility

RAM Ratings Lanka's chief concerns hinge on the fragility of these subsidiaries, and the resultant capital infusions that MBSL would be required to make. In aggregate, these injections are estimated to amount to about LKR 1.5 billion, and would increase MBSL's gearing ratio to 1.75 times. (end-March 2010: 1.12 times). However, our concerns are mitigated by the financial flexibility derived from MBSL's parent and the leeway it has to gear up further to the regulatory cap of 7 times.

Going forward, the Company intends to strengthen its presence in the micro-financing segment and broadly align itself with national development objectives. Under the new Chairman's stewardship, aggressive expansion into new business lines is unlikely in the medium term.

Corporate Governance

MBSL's 8-member board had met monthly during the reviewed period. The board comprises 2 nominees from BOC and 6 independent directors, who are assisted by 7 committees: audit, compensation, credit, purchasing, incentive, training, and investment. Subsequent to the appointment of the new chairman, a new board was also appointed; Mr JGBP Tissera was not re-elected while Mr. Lalith De Silva was newly appointed.

Weak asset quality

Asset mix reflects liquid stance

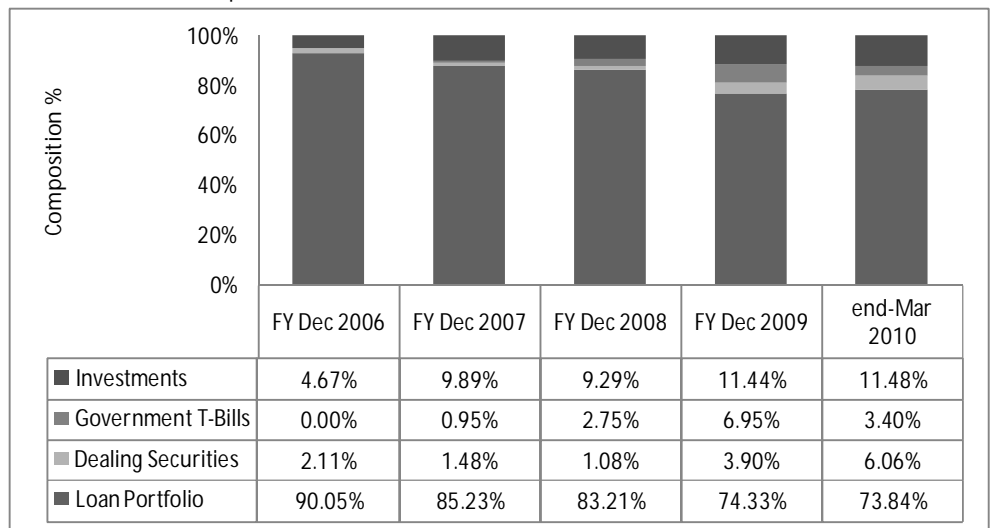
Marginal growth in loan portfolio

Asset Quality

RAM Ratings Lanka opines that MBSL's asset quality is weak; the Company's gross NPL ratio has remained higher than the overall industry, albeit having eased in FY Dec 2009. The improvement had been primarily due to recoveries and loan write-offs. In this regard, we acknowledge the management's initiatives to strengthen recoveries. Going forward, the Company's asset quality is expected to be maintained at current levels – and remain weaker than the industry over the short to medium term.

MBSL's asset base expanded 17.00% year-on-year ("y-o-y") to LKR 5.58 billion as at end-FY Dec 2009. The expansion had been mainly fuelled by investments in subsidiaries, government securities and equity investments. As such, the increased investments in dealing securities had tilted the Company's asset mix towards a more liquid stance (refer to Chart 2).

Chart 2: Asset composition



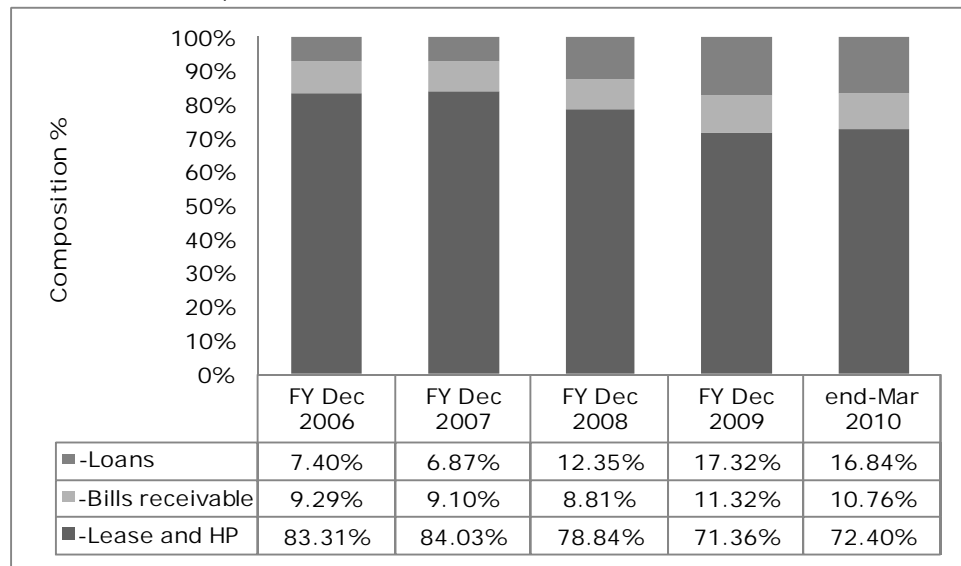
*Investments – Investments in subsidiaries, Associates and investment properties

Source: MBSL annual report

Meanwhile, the Company's total loan portfolio grew by a marginal 2.60% to LKR 4.37 billion as at end-FY Dec 2009 (industry growth: -6.18%); the portfolio expanded further to LKR 4.42 billion by end-March 2010. The loan growth during the review period was driven primarily by other advances, which mainly comprised term loans. However, we note that the MBSL's lease and HP portfolio, which was the core segment of loans, contracted 7.03% y-o-y to LKR 3.17 billion, in line with the non conducive economic climate that prevailed during the year (refer to Chart 3).

Gross NPL ratio-
improving albeit
weak

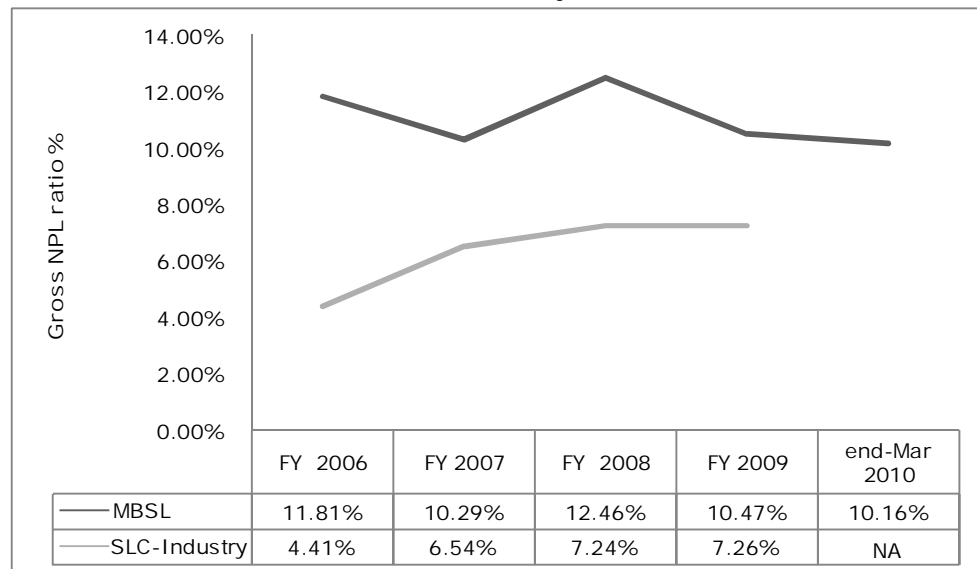
Chart 3: Loan composition



Source: MBSL annual report

MBSL's gross NPL ratio had eased during the reviewed period, albeit still weaker than the industry's. The Company's gross NPL ratio ameliorated from 12.46% as at end-FY Dec 2008 to 10.47% as at end-FY Dec 2009, improving further to 10.16% as at end-March 2010 (refer to Chart 4). This had been mainly driven by LKR 341.48 million of recoveries on the back of the management's efforts to rein in NPLs, together with LKR 50.33 million of loan write-offs. Meanwhile, we note that the level of absolute NPLs in the Company's key lease and HP portfolios as well as other loans had also improved, supported by strong recoveries. However, delinquencies in its bills portfolio had worsened over the same period.

Chart 4: Gross NPL ratio - MBSL vs the industry



Source: Central Bank of Sri Lanka, CBSL annual report

Adequate
provisioning

RAM Ratings Lanka deems MBSL's provisioning to be adequate, and better than its peers'. In addition to the Central Bank's regulations on provisioning for bad and doubtful debts, MBSL also adopts its own hair-cut rule with regard to the netting off of immovable property for the purpose of provisioning, which we believe to be more stringent. That said, the Company's gross NPL coverage ratio deteriorated from 60.72% as at end-FY Dec 2008 to 58.19% as at end-FY Dec

Increased investments in equity

2009, due to write-offs against provisions. However, recoveries in the first 3 months of this year resulted in an improved gross NPL coverage ratio of 62.44% as at end-March 2010.

On a separate note, in line with the buoyancy of the equity market, MBSL had increased its exposure to this segment. Its equity share portfolio had augmented to LKR 217.43 million as at end-FY Dec 2009 (end-FY Dec 2008: LKR 51.51 million), and further to LKR 341.63 million by end-March 2010; this accounted for 6.06% of the Company's total assets as at the same date (end-FY Dec 2009: 3.90%). While we note that increased exposure to equity introduces market risk, our concerns are mitigated by the Company's well-diversified and liquid share portfolio. Additionally, the management has placed a cap of LKR 500 million on MBSL's equity exposure.

Moderate performance, weighed down by high interest costs

Performance

MBSL's performance has been moderate; heightened interest expenses on increased borrowings had squeezed its net interest income in FY Dec 2009. However, this had been compensated by non-interest income, primarily from the disposal of investment properties and gains on dealing securities. Going forward, MBSL's performance is anticipated to improve in line with the more favourable macroeconomic conditions and loan expansion.

Receding interest income

The Company's interest income crept up 1.58% y-o-y to LKR 982.55 million in FY Dec 2009, compared to a 25.57% growth the preceding year. The slowdown was primarily due to the contraction in its lease and HP portfolio during the review period. Meanwhile, MBSL's interest expenses increased at a faster pace of 6.73% in FY Dec 2009, owing to additional borrowings.

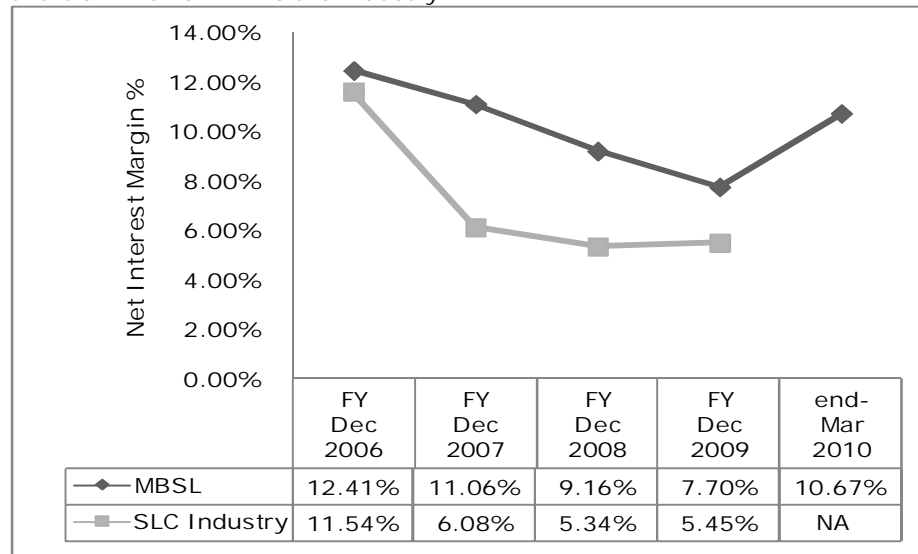
Thinner net interest income reduced NIM

Consequently, MBSL's net interest income contracted to LKR 398.30 million in FY Dec 2009 (FY Dec 2008: LKR 419.92 million). This translated into a relatively lower net interest margin ("NIM") of 7.70%, albeit stronger than the industry average (refer to Chart 5). However, we note that the Company's NIM had broadened to 10.67% as at end-March 2010, driven by the substitution of relatively high-cost borrowings with more favourable short-term facilities due to low short-term interest rates.

Healthier non-interest income

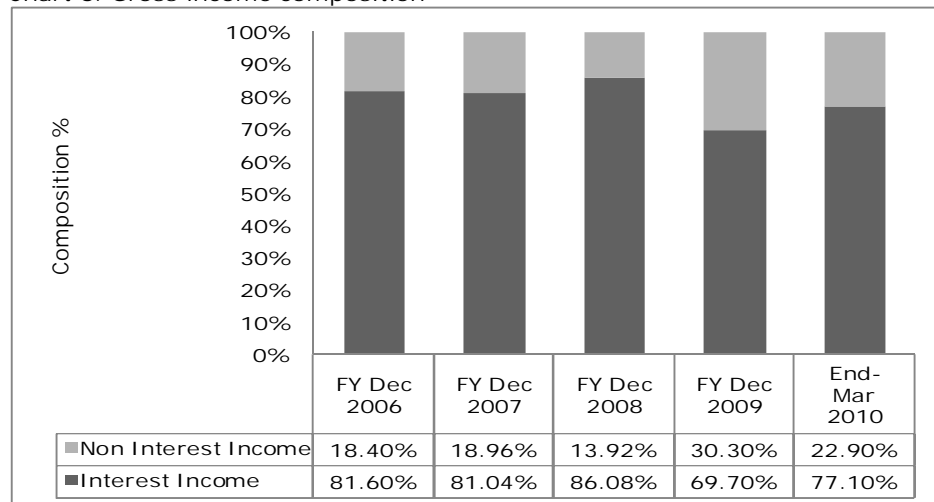
On a separate note, MBSL's non-interest income had augmented by LKR 105.27 million to LKR 173.19 million during the reviewed period, mainly a result of capital gains on the disposal of an investment property and profits from its portfolio of dealing securities. Consequently, the Company's gross income had tilted towards non-interest income (refer to Chart 6).

Chart 5: MBSL's NIM vs the industry



Source: Central Bank of Sri Lanka, MBSL annual report

Chart 6: Gross income composition



Source: MBSL annual report

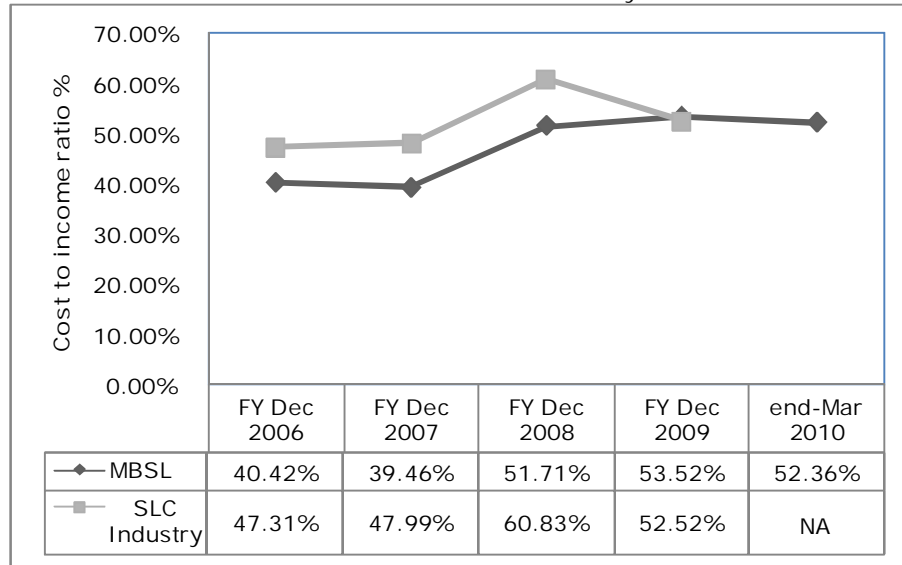
Moderate cost management

MBSL's cost management remained moderate, with a cost-to-income ratio of 53.52% as at end-FY Dec 2009. This was marginally weaker than the industry's level as at the same date (refer to Chart 7). However, MBSL's cost-to-income ratio was seen to plateau to 52.36% as at end-March 2010. Increased provision charges amounting to LKR 74.44 million also weighed down its performance last year.

Strengthening ROA

Higher reliance on short-term funds

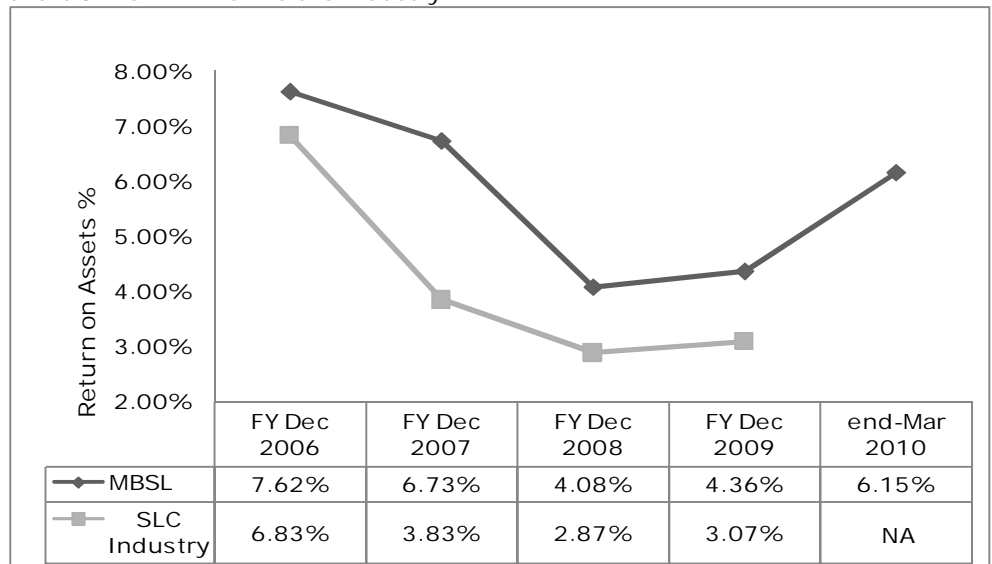
Chart 7: Cost-to-income ratio – MBSL vs the industry



Source: Central Bank of Sri Lanka, MBSL annual report

Overall, the Company's pre-tax profit advanced by LKR 50.85 million to LKR 254.26 million in FY Dec 2009. This translated into a Return on Assets ("ROA") of 4.36% as at the same date, which was stronger than the industry average (refer to Chart 8). MBSL's ROA had strengthened to 6.15% by end-March 2010, supported by a healthier NIM and improved asset quality, which had reduced its provision charges.

Chart 8: ROA – MBSL vs the industry



Source: Central Bank of Sri Lanka, MBSL annual report

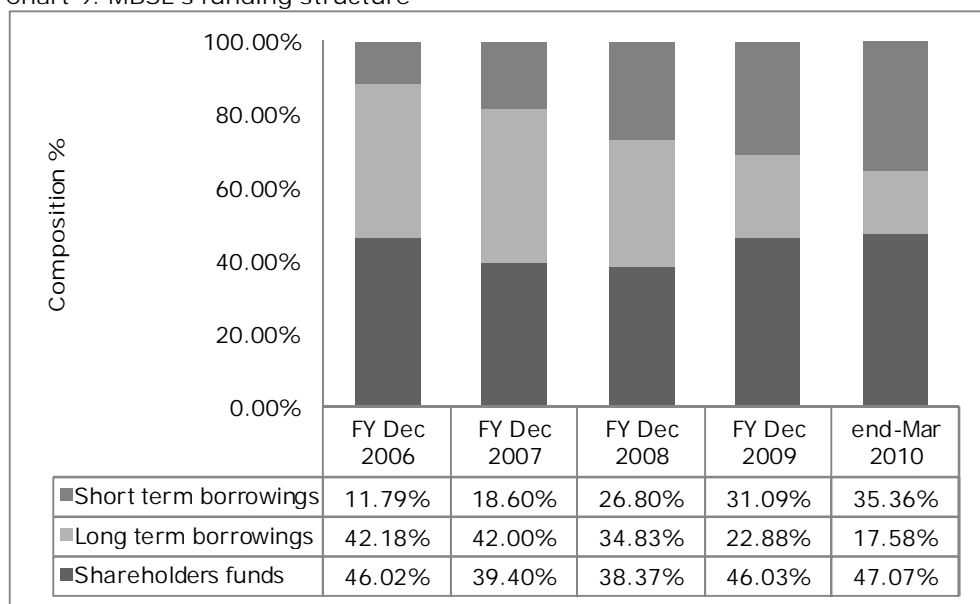
Funding & Liquidity

As highlighted in the previous review, MBSL had increased its reliance on short-term borrowings, which accounted for 35.36% of its total funding as at end-March 2010. RAM Ratings Lanka's concerns hinge on MBSL's future funding commitments to its recently acquired subsidiaries. That said, our concerns are somewhat mitigated by the financial flexibility derived from its parent's support.

Funding mix tilt towards short term debts

Shareholders' funds continued to dominate MBSL's funding mix in FY Dec 2009, when the Company strengthened its capital further via a LKR 540 million rights issue. That said, we note that the company tilted towards short-term borrowings in FY Dec 2009 (refer to Chart 9). In line with the environment of receding interest rates, MBSL had sought to substitute its relatively costly long-term borrowings with more attractive short-term facilities. As such, the Company had increased its borrowings via commercial papers, to LKR 1.34 billion as at end-March 2010 (end-FY Dec 2008: LKR 382.41 million). In line with its heftier short-term borrowings, the Company's asset-liability mismatch also narrowed in FY Dec 2009, from 22.69% to 7.25% of total interest earning assets in the "less than 1 year" bucket. While this would have a favourable impact on its performance, such significant dependence on short-term funding may expose the Company to liquidity risk in the short to medium term.

Chart 9: MBSL's funding structure



Source: MBSL annual report

Capital infusions required by subsidiaries

Going forward, MBSL will be required to infuse capital to support its recently acquired ailing subsidiaries. MBSL Savings will need a capital infusion of LKR 1.43 billion by end-December 2012, in order to comply with the minimum regulatory requirement. Initial plans are already in place to bolster the capital of MBSL Savings via a non-voting share issue during the course of this year. Elsewhere, capital infusions may also be required by MBSL Insurance in the short to medium term, to prop up its financial position. These injections are expected to increase MBSL's gearing level to 1.75 times, although still well below the regulatory maximum of 7 times. In addition, we derive comfort from the Company's LKR 600 million of unutilised funding lines from its parent.

Capital Adequacy

RAM Ratings Lanka opines that MBSL is adequately capitalised, with LKR 2.33 billion of shareholders' funds as at end-FY Dec 2009; this accounted for a sturdy 41.78% of the Company's total assets as at the same date. We also derive comfort from BOC's parental support, recently demonstrated when it subscribed for the Company's rights issue in December 2009.

Industry Overview

Sri Lanka's gross domestic product ("GDP") expanded 3.5% in 2009 (refer to Table 1). Although this was weaker than the 6.0% growth attained in 2008, the slower growth has to be put in the context of the global downturn. Not surprisingly, all 3 major sectors (i.e. Agriculture, Industrial and Service) of the Sri Lankan economy have been hit by the global upheaval.

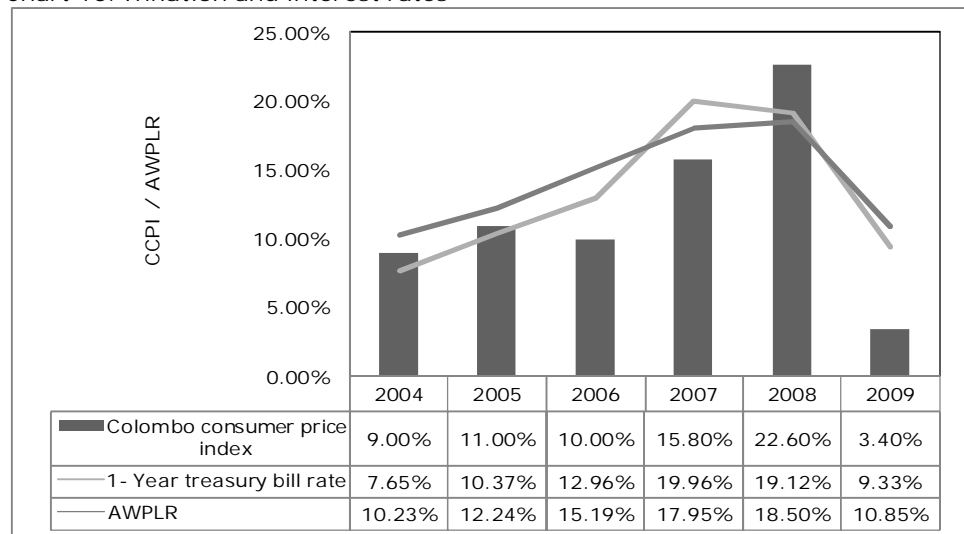
Table 1: GDP composition

Sector	2008	2009
Agriculture, forestry and fishing	7.5%	3.2%
Industrial	5.9%	4.2%
Services	5.6%	3.3%
GDP	6.0%	3.5%

However, the end of the 25-year war against the separatist Tamil Tigers together with the stand-by arrangement from the International Monetary Fund ("IMF") helped revive economic activity. During six months ended FY Dec 2009, performance of the island's primary sectors had been hampered by droughts, weaker prices, subdued local appetite and receding world demand. Industry and services sectors grew by 2.4% and 1.1% respectively in 1H 2009, comparing weaker to the previous year's 6.5% and 6.7%. Nonetheless, onset of peace and easing monetary policies spurred allowed these two sectors to post stronger growth rates of 5.9% and 5.4% in 2H 2009 (2H 2008: 5.4%, 4.7%). Going forward, GDP growth for 2010 is expected to clock in at 6.0%, which is significantly higher than 3.5% recorded for 2009.

Furthermore, interest rates have dipped sharply in tandem with the Central Bank's loosened monetary policy (refer to Chart 10). While continually lower interest rates may not be sustainable given the country's budget deficit, RAM Ratings Lanka also notes that interest rates will not revisit the highs of 2008. On the whole, however, we envisage the credit cycle to chart a rising trend.

Chart 10: Inflation and interest rates



Source: Central Bank of Sri Lanka

Against this backdrop, leasing companies took up 2.3% of total financial assets as at end-December 2009. The environment of high interest rates dampened

demand and thus the entire leasing sector. Leasing companies face a dilemma as they were precluded from obtaining public funds, and have to depend on bank funding to finance their lending activities. Even though the Finance Leasing ACT was amended to raise funds from the public by issuing debt instruments, RAM Ratings does not expect the benefits to materialise in the near term. However, inline with the easing interest rate scenario, we expect consumer demand to bounce back; the recent reduction in vehicle taxes is also expected to support top line growth.

As such, going forward, SLCs are envisaged to post healthier results over the medium term. Interest income is expected to improve owing to the higher demand, while interest expenses are anticipated to recede. Nonetheless, over the short term, companies incur losses in disposing existing seized stock, following the reduction in import taxes of vehicles.

In terms of asset quality, RAM Ratings Lanka opines defaults across the industry to ebb with the improvement in macroeconomic environment. Defaults spiked the previous year, as rising inflation eroded purchasing power, straining the borrowers' repayment capacity.

Meanwhile, competition from commercial banks has become keener as they have also ventured into the leasing arena, i.e. the key business segment of leasing companies. In this respect, leasing companies compete against banks by providing customised and swift service. Moving forward, the prospects of leasing companies will be dictated by franchise, service quality and innovative business strategies.

Corporate Information

Date of Incorporation:	1982			
Commencement of Business:	1982			
Major Shareholders:	Bank of Ceylon		72.14%	
	Bank of Ceylon A/C Ceybank Unit Trust		3.34%	
	Green Care International Limited		1.76%	
	Prime Lands (Pvt) Ltd		1.60%	
	Distilleries Company of Sri Lanka Limited		0.71%	
Directors:	Mr MR Shah		Chairman	
	Ms WA Nalani		Director	
	Mr. M S S Paramananda		Director	
	Mr. Lakshman Perera		Director	
	Mr. P G Rupasinghe		Director	
	Mr V Kanagasabapathy		Director	
	Dr. Ranjith Bandara		Director	
	Mr. Lalith De Silva		Director	
Auditor:	SJMS Associates Chartered Accountants			
Listing:	1991			
Key Management:	Mr Gamini Karunathilake	Chief Executive Officer		
	Mr Ranjith Siriwardena	Deputy Director – Strategic Planning & Risk Management		
	Mr.Senaka Udawalawa	Assistant Director – Leasing and Administration		
	Mr Lakshman Kaluarachchi	Deputy Director – Leasing		
	Ms Shyamalie Amaratunga	Deputy Director – Trade Finance		
	Mr AMA Cader	Deputy Director – Corporate Advisory & Capital Markets		
	Mr Priyantha Herath	Assistant Director – Finance & Treasury		
	Mrs Marina Phillips	Company Secretary		
Major Subsidiaries and Associates:	Merchant Credit of Sri Lanka	51.00%		
	Lanka Securities Limited	29.00%		
	Mega Containers Ltd	18.30%		
	MBSL Savings Bank	78.00%		
	MBSL Insurance	100.00%		
Capital History	Year	Remarks	Amount (LKR million)	Cumulative Total (LKR million)
	1989	Ordinary share capital	25.00	25.00
	1990	Share issue	65.00	90.00
	1991	Rights issue	60.00	150.00
	1993	Rights issue	130.00	280.00
	1994	Bonus issue	220.00	500.00
	2004	Write off of losses	(270.00)	230.00
	2004	Conversion of preference shares to ordinary shares	370.00	600.00
	2005	Rights issue	300.00	900.00
	2007	Capitalisation of share premium	167.00	1067.00
	2009	Rights Issue	540.00	1607.00

Financial Summary - Company

	Unaudited				
BALANCE SHEET (LKR million)	31-Dec-06	31-Dec-07	31-Dec-08	31-Dec-09	31-Mar-10
Property, Plant and Equipment	27.16	25.53	32.24	39.27	40.02
Investment in Associates/Subsidiaries	56.94	95.54	103.90	354.55	363.59
Other Investments/Investment Properties	106.79	340.16	339.09	283.76	283.28
Gross Debtors	3,353.34	3,998.97	4,257.65	4,368.42	4,417.89
Leasing & Hire Purchase	2,815.57	3,387.71	3,405.31	3,165.79	3,237.91
Others	537.77	611.26	852.34	1,202.63	1,179.98
Estimated Residual Values					
Less : Deposits					
Less : Loan Loss Reserves	(239.19)	(274.15)	(322.05)	(266.06)	(280.18)
Net Debtors	3,114.15	3,724.82	3,935.60	4,102.36	4,137.71
Amounts due from Holding/Related Companies					
Other Loans & Advances					
Cash and Bank Balances	1.42	0.31	38.24	39.51	69.72
Other Current Assets	197.24	217.72	319.08	759.48	741.23
TOTAL ASSETS	3,503.70	4,404.08	4,768.15	5,578.93	5,635.55
Long Term Deferred Liabilities	127.27	101.32	81.91	82.32	83.82
Redeemable Hybrid Capital					
Long Term Private Debt Securities					
Less : Sinking Fund					
Other Long Term Loans	1,298.10	1,667.86	1,524.83	1,158.54	897.29
Total Long Term Debt	1,298.10	1,667.86	1,524.83	1,158.54	897.29
Short Term Private Debt Securities	362.87				
Amounts due to Holding/Related Companies					
Other Short Term Loans	73.91	822.68	1,200.390	1,586.34	1,805.13
Total Short Term Debt	436.780	822.68	1,200.39	1,586.34	1,805.13
Trade Creditors					
Provision for Dividend					
Provision for Taxation					
Other Current Liabilities	225.300	247.50	281.22	420.96	446.34
TOTAL LIABILITIES	2,087.45	2,839.36	3,088.35	3,248.16	3,232.58
Equity Share Capital	900.00	1,067.00	1,067.00	1,607.00	1,607.00
Irredeemable Hybrid Capital					
Reserves	181.67	31.36	45.72	59.78	59.78
Less : Intangible Assets					
Retained Profit/(Loss)	334.58	466.36	567.08	663.99	736.19
Minority Interests (MI)					
TOTAL SHAREHOLDERS' FUNDS + MI	1,416.25	1,564.72	1,679.80	2,330.77	2,402.97
TOTAL LIABILITIES + SHAREHOLDERS' FUNDS + MI	3,503.70	4,404.08	4,768.15	5,578.93	5,635.55

Financial Summary - Company

	Unaudited				
INCOME STATEMENT (LKR million)	31-Dec-06	31-Dec-07	31-Dec-08	31-Dec-09	31-Mar-10
Interest Income	609.52	770.34	967.30	982.55	256.33
Less : Interest Expense	(189.02)	(333.20)	(547.39)	(584.25)	(106.80)
Net Interest Income	420.50	437.13	419.91	398.30	149.53
Non-interest Income	94.84	102.26	67.92	173.19	44.42
Gross Income	515.34	539.39	487.83	571.49	193.95
Less : Non-interest Expenses	(208.49)	(226.83)	(245.24)	(263.08)	(101.55)
Less : Bad & Doubtful Debt Provisions	(38.91)	(37.36)	(47.90)	(74.44)	(3.75)
Less : Depreciation & Amortisation	(9.79)	(9.07)	(7.76)	(8.21)	(2.49)
Operating Profit/(Loss) Before Tax	258.15	266.13	186.93	225.76	86.16
Share in Results of Associated Companies	11.03	7.14	16.47	28.50	13.84
Prior Year Adjustments					
Exceptional Items					
Adjusted Profit/(Loss) Before Tax	269.18	273.27	203.40	254.26	100.00
Less : Tax	(59.64)	(34.80)	1.66	(53.29)	(27.79)
Adjusted Profit/(Loss) After Tax	209.54	238.47	205.06	200.97	72.21
Extraordinary Items					
Less : Transferred to Statutory Reserve					
Less : Dividends	(67.50)	(90.00)	(90.00)	(90.00)	
Retained Profit/(Loss) For The Year	142.04	148.47	115.06	110.97	72.21
CASH FLOW STATEMENT (LKR million)	31-Dec-06	31-Dec-07	31-Dec-08	31-Dec-09	31-Mar-10
Cash Flow From Operating Activities	(181.33)	(344.05)	(89.35)	52.99	(24.08)
Cash Flow From Investing Activities	(26.26)	(268.25)	15.11	(279.99)	(111.33)
Cash Flow From Financing Activities	(226.25)	464.79	216.34	705.85	(116.17)
Net Increase/(Decrease) in Cash During The Year	(433.84)	(147.51)	142.10	478.85	(251.58)
Cash Balance at Beginning of the Year	373.39	(60.45)	(207.96)	(65.86)	412.99
Cash Balance at End of the Year	(60.45)	(207.96)	(65.86)	412.99	161.41

Financial Ratios – Company

KEY RATIOS	31-Dec-06	31-Dec-07	31-Dec-08	31-Dec-09	31-Mar-10
Profitability (%)					
Net Interest Margin	12.41%	11.06%	9.16%	7.70%	* 10.67%
Cost/Income Ratio	40.42%	39.46%	51.71%	53.52%	52.36%
Return on Average Assets	7.62%	6.73%	4.08%	4.36%	* 6.15%
Return on Average Equity	19.19%	17.86%	11.52%	11.26%	* 14.56%
Capitalisation (times)					
Gearing Ratio	1.22	1.59	1.62	1.18	1.12
Long Term Gearing Ratio	0.92	1.07	0.91	0.50	0.37
Short Term Gearing Ratio	0.31	0.53	0.71	0.68	0.75
Capital Adequacy Ratio (%)	42.03%	37.23%	36.73%	38.84%	39.78%
Coverage (times)					
Interest Coverage Ratio	2.42	1.83	1.36	1.40	1.83
Asset Quality (%)					
Gross NPL	11.81%	10.29%	12.46%	7.00%	10.16%
Loan Loss Reserve Coverage	7.13%	6.86%	7.56%	6.09%	6.34%
General Loan Loss Reserve Coverage	2.42%	2.51%	2.30%	2.28%	2.33%
Loan Loss Reserve Coverage (Gross NPL)	60.42%	66.62%	60.72%	58.19%	62.44%

NOTES:

* annualised

* Negative ratios are due to negative net asset prevailed during the respective financial years.

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

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.
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.

For long-term ratings, RAM Ratings 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.

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.
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.

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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>

