Lanka Rating Agency

Rating Report

Orient Finance PLC

Report Contents

Rating History

Dissemination Date	Long Term Rating	Outlook	Action	Rating Watch
11-Oct-2024	BB+	Positive	Initial	-

Rating Rationale and Key Rating Drivers

Orient Finance PLC ("OFL" or "the Company") is a listed Leasing Finance Company (LFC) principally involved in financial activities including mobilization of deposits, savings accounts, leasing, hire purchase, gold loans, pledge loans, and factoring. The market share of the Company remains restricted (~1%) representing sufficient room for business expansion complemented by a consolidation scheme at the industry level and rising competition. Historically, the company's financial performance indicators reflected a volatile pattern with fragility in profitability owing to dwindled asset quality and rising NPAs. However, the company's risk profile is now steered towards a turnaround trajectory with improved asset quality and gross NPAs (~12.0%): this is below the industry average ratio (~14.7%). Consequently, the profit after tax (PAT) for FY24 increased to ~LKR 349 mln compared to FY23 a loss of ~LKR 72 mln, but there is still room for improvement. The presence of key group management personnel at Orient Finance has boosted the company’s operational efficiency. The company's current portfolio is concentrated towards leasing with a (~65%) focus. Although a shift in the lending portfolio towards the gold loans (~31%) is observed. On the other hand, with the Central Bank of Sri Lanka (CBSL) amalgamation program coming into play, the company is currently considering a possible merger or acquisition of another financial entity, the outcome of which is yet to materialize. The ratings also take into account improved governance and operational practices set out to support the efficacy of business processes which would ultimately translate into better financial performance.

The assigned "Positive Outlook" reflects the Company's improved performance indicators. Continuation of the growth momentum and sustenance of strong key performance and financial indicators are essential for an upgrade consideration. In addition, improvement in core income and rationalization of administrative expenses are imperative as the Company consolidates its position. The management's ability to increase and retain its market share and diversify its revenue base to improve its competitive position in the industry of non-banking finance companies is critical. Retention of key personnel, adherence to regulatory requirements, and sustainability of profitability will remain imperative to uphold the ratings.

Disclosure

Name of Rated Entity	Orient Finance PLC
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Non-Banking Financial Institution Rating(Jul-24)
Related Research	Sector Study | Leasing & Finance Companies(Aug-23)
Rating Analysts	Imran Iqbal | imran@lra.com.lk | +94 114 500099

Profile

Structure Orient Finance PLC ("OFL" or "the Company") is a public limited company established in 1981. The company listed its business on the Colombo Stock Exchange (CSE) in 2011.

Background Orient Finance PLC was initially set up in 2003 as a specialized leasing company to provide leasing facilities to United Motors Lanka PLC. The company later converted to a licensed finance company in 2011 and listed its shares on the CSE. As part of the consolidation program of the Central Bank of Sri Lanka (CBSL) in 2014, Bartleet Finance which commenced business in 1981, was acquired by Janashakthi Holding Limited and merged with Orient Finance. Special approval was obtained from the CBSL to name the merged entity "Orient Finance PLC".

Operations The company is principally involved in financial activities including mobilization of deposits, savings accounts, leasing, hire purchase, gold loans, pledge loans and factoring

Ownership

Ownership Structure Janashakthi Holding owns (~93%) of the shares of the Company. The second major shareholder, First Capital PLC accounts for (~1%) of the total shares.

Stability The Company is proceeding on a path of growth, in terms of financial assets on sound footings. A generally prudent approach is adopted by the Sponsors in its prospective expansion plans.

Business Acumen Apart from the Company, the Sponsors have a strategic stake in other sectors as well, thus the business acumen is considered strong.

Financial Strength The financial strength of Sponsors is considered adequate as Janashakthi Limited possessed an asset base of over ~LKR165.1bln as of CY23.

Governance

Board Structure The Company's board comprises of 10 members. Including the Chairman, board has 1 Executive Director, 2 Non-Independent Non-Executive Directors and 7 Independent Non-Executive Director.

Members' Profile The board members' areas of expertise include banking, manufacturing, leasing, and law. They offer a multitude of expertise in various fields.

Board Effectiveness The board has established five board-level committees, namely; the Audit Committee, Human Resources and Remuneration Committee, Integrated Risk Management Committee, Related Party Transactions Review Committee and Nomination Committee.

Financial Transparency BDO Partners is the External Auditor of the Company. They have expressed an unqualified opinion on the Company's Financial Statements for FY24. The Audit Committee directly oversees the internal audit function, with a review of financial statements and smooth progression.

Management

Organizational Structure The management of the Company is based on a team of seasoned professionals who have served in both banking and non-banking financial institutions over a long tenure. The operations are divided into thirteen functional departments. The reporting lines of all departments converge towards the CEO, with Internal Audit, Compliance and Risk departments reporting both to the CEO as well as the Board Audit Committee & Integrated Risk Management Committee.

Management Team The Company's management team is headed by its CEO, K.M.M.Jabir, who has 36 years of vast experience in the Finance and Banking industry. The Directors and CEO are assisted by a seasoned team of professionals with over a decade of experience.

Effectiveness There are currently three management committees in place, namely, i) Credit Committee, ii) Liquidity Committee, and iii) Assets and Liability Management Committee, which meets on a monthly basis to discuss the overall performance of the company, KPIs, and strategies.

MIS The Company has invested in upgradation and modernization of its IT infrastructure. The Company maintains a primary data center at Pitipana and a disaster recovery site at SLT Lotus Road.

Risk Management Framework The Company manages its risks in a prudent manner. Risk is managed through monitoring and controlling operational and strategic activities of Orient Finance PLC in terms of credit, liquidity, operational, and market risk. A comprehensive risk management framework is adopted by the Company.

Business Risk

Industry Dynamics At present, there are 33 LFCs in Sri Lanka, of which 28 are listed on the Colombo Stock Exchange. By the end of March 2024, the profit after tax (PAT) of LFCs in Sri Lanka increased by 51% to LKR 51.4 Bn, compared to LKR 34.0 Bn recorded in the corresponding period of the previous year. This substantial increase was primarily driven by higher interest income, coupled with reduced impairment charges for loan losses.

Relative Position The Company is considered a small player in the industry accounting for 1% of assets in FY24 and 1% of deposits in the LFC and specialized leasing company sector. In addition, the company loans and advances represented 1% in FY24 in LFC and the specialized leasing company sector. The Company is operating with a branch network of 35 Branches which includes 4 new branches that were added during FY24.

Revenues Gross Interest Income during FY24 stood at ~LKR 4.6Bn which is mainly driven by leasing income and gold Loans. Orient Finance PLC's main focus is to maintain its lending portfolio dominated by Leases. During FY24 net interest income was recorded at ~LKR 1.8 Bn which is an increase of ~81%.

Performance The financial performance of the company showed progress, as the revenue boost gained further momentum through sustained financial costs and reduced overhead costs, converging into a profit for the year of ~LKR 349 mln in FY24. In FY23 the Company recorded a loss for the year of ~LKR 72 mln.

Sustainability According to the forecasted results, the company expects growth in leases, loans, and advances of 55% in FY25, 46% in FY26, and 9% in FY27. This growth is considered after taking into account the improvement in the tourism industry, the restriction on the importation of vehicles which has increased the prices of second-hand vehicles and transportation services, including SME working capital support.

Financial Risk

Credit Risk The company gross non-performing loans has increased over the period from 10.2% in FY23 to 12.0% in FY24.This is a marginal increase of ~18%.

Market Risk The company's investment portfolio consists of investments in fixed deposits, Government securities, Investment Quoted – Quoted, and unquoted and investments property.

Liquidity And Funding The company's main source of funding remains deposits and bank borrowings. Orient Finance PLC maintains a fairly healthy funding structure, leveraging stood at 13.2% FY24 (FY23: 19.1%, FY22: 27.3%). Deposits are predominantly by individual depositors.

Capitalization The Company's Capital Adequacy Ratios ("CAR") as at 31 March 2024 were 15.22% (2023 - 15.50%) and 15.63% (2023 - 16.58%) for Tier 1 Capital and Total Capital respectively. CAR is above the CBSL statutory requirement of 12.5%.

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#	Jun-24	Mar-24	Mar-23	Mar-22
#	3M	12M	12M	12M
A BALANCE SHEET				
1 Total Finance-net	15,661	14,768	12,558	11,774
2 Investments	1,727	1,665	1,964	1,397
3 Other Earning Assets	1,161	343	236	242
4 Non-Earning Assets	2,774	2,810	2,328	1,962
5 Non-Performing Finances-net	945	891	383	2,352
Total Assets	22,267	20,477	17,469	17,727
6 Funding	17,796	15,966	13,653	13,836
7 Other Liabilities	779	909	535	559
Total Liabilities	18,575	16,874	14,188	14,395
Equity	3,692	3,603	3,281	3,332
B INCOME STATEMENT				
1 Mark Up Earned	1,058	4,602	3,593	2,709
2 Mark Up Expensed	(555)	(2,807)	(2,600)	(1,159)
3 Non Mark Up Income	58	267	227	263
Total Income	561	2,061	1,220	1,813
4 Non-Mark Up Expenses	(370)	(1,371)	(1,140)	(1,085)
5 Provisions/Write offs/Reversals	(63)	(140)	(103)	(125)
Pre-Tax Profit	129	550	(23)	603
6 Taxes on Financial Services	(40)	(201)	(49)	(150)
Profit Before Income Taxes	89	349	(72)	453
7 Income Taxes	-	-	-	-
Profit After Tax	89	349	(72)	453
C RATIO ANALYSIS				
1 PERFORMANCE				
a Non-Mark Up Expenses / Total Income	65.9%	66.5%	93.4%	59.9%
b ROE	9.8%	10.1%	-2.2%	13.6%
2 CREDIT RISK				
a Gross Finances (Total Finance-net + Non-Performing Advances + Non-Performing Debt Instruments) / Funding	100.0%	105.1%	102.4%	108.9%
b Accumulated Provisions / Non-Performing Advances	55.9%	55.9%	73.1%	28.5%
3 FUNDING & LIQUIDITY				
a Liquid Assets / Funding	13.6%	10.6%	13.2%	9.1%
b Borrowings from Banks and Other Financial Institutes / Funding	10.9%	13.2%	19.1%	27.3%
4 MARKET RISK				
a Investments / Equity	46.8%	46.2%	59.9%	41.9%
b (Equity Investments + Related Party) / Equity	0.0%	0.0%	0.3%	1.5%
5 CAPITALIZATION				
a Equity / Total Assets (D+E+F)	16.6%	17.6%	18.8%	18.8%
b Capital formation rate (Profit After Tax - Cash Dividend) / Equity	9.9%	10.6%	-2.2%	13.6%

Credit Rating

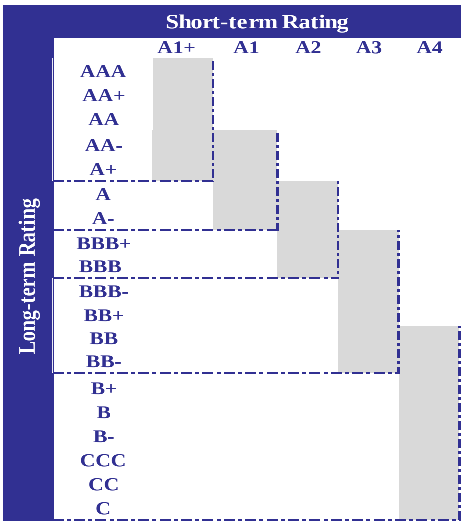
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short-term Rating

Scale	Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

a) Broker Entity Rating
b) Corporate Rating
c) Debt Instrument Rating
d) Financial Institution Rating
e) Holding Company Rating
f) Independent Power Producer Rating
g) Microfinance Institution Rating
h) Non-Banking Finance Companies Rating

Rating Team Statements
(1) Credit Rating Agency means a body corporate engaged in the business of assessing and evaluating the credit- worthiness of any issuer or a specific issue of securities. https://www.sec.gov.lk/credit-rating-agency/

Conflict of Interest
(2) i. LRA will disclose to the Commission all other business activities it is engaged in at the time of applying for its licence and inform the Commission in writing prior to engaging in any other business activity after obtaining a licence from the Commission. (Section 34 – Rules applicable to Credit Rating Agencies)
(2) ii.LRA will not engage in any other business which in the view of the Commission creates a conflict of interest unless prior written approval of the Commission is obtained. (Section 35 – Rules applicable to Credit Rating Agencies)
(2) iii.In the conduct of any such other business activity, the LRA will ensure that proper processes are in place to have a clear demarcation of the different functions pertaining to such businesses. (Section 36 – Rules applicable to Credit Rating Agencies)

Restrictions
(3) (i) LRA will not be outsource any part of its work, which has a direct bearing on the function of rating. (Section 24 – Rules applicable to Credit Rating Agencies)
(3) (ii) LRA will enter into a written agreement with the party to whom any work is outsourced. Such agreement contains an undertaking from the party to whom any work is outsourced that they shall comply with the laws, rules, and directives that the LRA is bound to follow. (Section 25 – Rules applicable to Credit Rating Agencies)

(4) The LRA will not appoint any individual as a member of the rating committee who:
(a) has a business development function of the Credit Rating Agency; or
(b) who initiates or participates in discussions regarding fees or payments with any Client of the LRA. (Section 28 – Rules applicable to Credit Rating Agencies)

Conduct of Business
(5) Prior to the commencement of a rating or during such process the LRA will not promise, assure or guarantee to a Client that a particular rating will be assigned. (Section 39 – Rules applicable to Credit Rating Agencies)

(6) LRA performs a rigorous and formal periodic review of all its methodologies. Such methodologies will be made available to the Commission for perusal, upon request. (Section 41 – Rules applicable to Credit Rating Agencies)

Independence & Conflict of interest
(7) LRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on LRA´s opinions or other analytical processes. In all instances, LRA is committed to preserving the objectivity, integrity, and independence of its ratings.

(8) LRA will not engage in any other business which in the view of the Commission creates a conflict of interest unless prior written approval of the Commission is obtained. (Section 35 – Rules applicable to Credit Rating Agencies)

(9) LRA will structure its rating teams and processes to promote continuity, consistency and avoid bias in the rating process. (Section 47 – Rules applicable to Credit Rating Agencies)

Monitoring and review
(10) For purposes of transparency the LRA will publish sufficient information about an entity/security rated, frequency of default and whether a rating grade assigned has changed over time. The definitions and computation methods for the default rates stated in the default studies shall also be disclosed. (Section 44 – Rules applicable to Credit Rating Agencies)

LRA maintain the following records pertaining to Clients:
(a) all internal records to support its credit rating opinions;
(b) all particulars relating to Clients at its office which shall include the name and registered address and contact numbers of such Client, names and addresses of their directors as at the date of rating, its issued share capital and the nature of business; and
(c) a written record of all complaints received from Clients and action taken thereon by the LRA. (Section 48 – Rules applicable to Credit Rating Agencies)

(11) LRA maintains confidentiality of all non-public information entrusted to it by Clients at all times including such Client's identity and transactions carried out for such Client unless and to the extent such disclosure is required by law, or unless authorised by the Client to disclose such information. (Section 50 – Rules applicable to Credit Rating Agencies)

(12) LRA does not destroy, conceal or alter any records, property or books relating to the business of the Credit Rating Agency which are in its possession or under its control with the intention of defeating, preventing, delaying or obstructing the carrying out of any examination (Section 53 – Rules applicable to Credit Rating Agencies)

Probability of Default
(13) LRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e., probability).

Proprietary Information