



Lanka Rating Agency

Rating Report

Asia Asset Finance PLC

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Rating History

Dissemination Date	Long Term Rating	Outlook	Action	Rating Watch
29-Oct-2024	-	-	Withdraw	-
27-Jan-2023	A-	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Subsequent to the management's decision to discontinue the rating, Lanka Rating withdraws the entity rating of Asia Asset Finance PLC with immediate effect

Disclosure

Name of Rated Entity	Asia Asset 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-24)
Rating Analysts	Gayani Randima Ariyawansa gayani@lra.com.lk +94 114 500099



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Profile

Structure Asia Asset Finance PLC ("the Company" or "AAF") is a public limited liability company incorporated and domiciled in Sri Lanka and listed on the Colombo Stock Exchange.

Background The Company was initially known as Finance and Land Sales Ltd and later acquired by Asia Capital PLC in 2004. It underwent changes for the Company name and renamed as Asia Asset Finance PLC. In 2014 AAF was acquired by Muthoot Finance Limited ("MFL") of India and it operates as the ultimate parent entity whose specialty is in Gold Loans.

Operations The principal activities of AAF are accepting deposits and giving loans and advances. The Company branch network consists of 75 branches as of FY23.

Ownership

Ownership Structure MFL holds the largest shareholding of AAF with 72.92% of the total stake. The second largest shareholder is Senthilveri Holdings (Pvt) Ltd (Seylan Bank – Margin Trading) with 10.01% and 6.63% is owned by J.B. Cocoshell (Pvt) Ltd.

Stability Muthoot Finance Ltd provides the mainstay for AAF operations. MFL has been increasing its shareholding since 2014 and it plans to hold it for long term which brings stability for the Company's shareholding.

Business Acumen MFL is the largest Gold Loan company in India and they have been operating the Gold Loan product for over 80 years successfully.

Financial Strength The Company does not have any guarantees or commitments from the parent company. MFL has an asset base of INR 830Bn for 9MFY24. MFL has injected cash through a rights issue to AAF. Although there is no written commitment, the previous track record shows that MFL is willing to inject cash if and when needed.

Governance

Board Structure The Board of the Company consists of eight members where three of them are Non-Independent and Non- Executives Directors and four are Independent and Non- Executive Directors as at the end of 31st March 2023. The remaining is the Chief Executive Officer.

Members' Profile The Company Board members in general, possess experience in many fields. Moreover, the members are equipped with relevant knowledge and years of experience in their respective industries. The Company Chairman Mr. V. A. Prasanth also holds an Independent, Non-Executive Directorship.

Board Effectiveness Asia Asset PLC consists of six board committees namely Audit Committee, Integrated Risk Management Committee, Remuneration Committee, Related Party Transactions Review, Credit & Recovery Committee, and IT Steering Committee.

Financial Transparency The external audit was carried out by BDO Chartered Accountants, and they issued an unqualified audit opinion with regarding the Company's annual financial statements for FY23.

Management

Organizational Structure The Company has a functional organizational structure. The CEO of the Company steers some key functions while the COO and GM handle the other functions both of whom report directly to the CEO.

Management Team The management team of the Company is steered by the CEO, Mr. Rajiv Gunawardena. He possesses overall 16 years of experience and qualifications. He has held the current position as CEO for about 12 years.

Effectiveness AAF has formed Assets & Liability Management Committee to manage various risks. The senior management and department heads meet bi-monthly.

MIS The Company uses "eFinancial solution" as the core system which is provided by Scierter Pte Ltd. The same vendor provides "Luck-eWallet" which is a mobile wallet and iMAS which is the ERP system solution that is provided in-house.

Risk Management Framework AAF has a formal risk management policy in place compiled by the Head of Risk Management. Integrated Risk Management Committee (IRMC) depicts a centralized functionality where Risk Management Department, Compliance Department, Policy & Planning Department, and Asset Liability Committee are descended from IRMC.

Business Risk

Industry Dynamics At present, there are 34 Licensed Finance Companies ("LFC") in Sri Lanka, out of which 27 are listed. The profitability of the sector dropped by ~47% in FY23 to LKR 31 Bn. The sector profitability as at 6MFY24 is recorded at LKR 16.4 Bn when compared to LKR 13 Bn in 6MFY23. The loan loss provisions increased by ~118% to LKR 13.5 Bn in FY23 (6MFY24: LKR 5.8 Bn). The total asset base of the LFC sector stood at LKR 1.64 Tn as at 6MFY24 (FY23: LKR 1.64 Bn, FY22: LKR 1.6 Mn). Subsequent to FY22, the asset quality deteriorated to a gross non-performing loan ("NPL") ratio of 16.01% as at FY23. However, as a result of the current macroeconomic challenges in the country, the gross and net NPL ratio deteriorated to 19.99% and 14.06% respectively as at 6MFY24.

Relative Position Asia Asset Finance PLC represents 1.55% of asset base with comparison to the industry in 6MFY24 (FY23: 1.53%). The Loans and advances portfolio of the Company demonstrates a slight decrease in the industry presence from 1.68% in FY23 to 1.56% in 6MFY24. Considering the focus on gold loans, the Company accounts for 6.65% of the industry pawning advances as at 6MFY24 and 7.12% as at FY24. The Company funding which recorded a significant amount from deposits and borrowings represent 1.46% and 3.5% respectively in 6MFY22 (FY23: 0.8% and 1.46%).

Revenues Net interest income has recorded a considerable increase of 39% in FY23 from LKR 1,252 Mn in FY22 (FY22: LKR1,252Mn). However, in 9MFY24 the net interest income illustrated a slight decline of -0.07% with comparison to 9MFY23 of LKR 1,341 Mn. The NIM was 6.67% in 9MFY24, and it was 8.94% in FY23. The interest income received from Gold Loans is significant, where it was 74.3% in 9MFY24 (FY22: 80.6%) which indicates the greatest contribution.

Performance In FY23 the Company has gained a YoY rise in profit after tax (PAT) of 149% to LKR 295 Mn from LKR 119 Mn in FY22. But PAT has slowed down in 9MFY24 by -2.3% (9MFY24: LKR 224 Mn, 9MFY23: LKR 229 Mn). In FY23 major expenses such as personnel expenses and general administration expenses were increased by 24% to LKR 414 Mn (FY22: LKR 333 Mn, 9MFY24: LKR 360 Mn) and 28% to LKR 853 Mn (FY23: LKR 664 Mn, 9MFY24: LKR 662 Mn) respectively. However, the key driving factor of rise in profit was mirrored in the growth in interest income in FY23 which recorded an increase of 109% to LKR 5,392 Mn (9MFY24: LKR 4,742 Mn). The Company ROE was recorded as 9.6% for the 9MFY24 (FY23: 10.2%, FY22: 4.8%). ROA has improved to 1.2 % in 9MFY24 (FY23: 1.3, FY22: 0.7%).

Sustainability In FY23 major expenses such as personnel expenses and general administration expenses were increased by 24% to LKR 414 Mn (FY22: LKR 333 Mn, 9MFY24: LKR 360 Mn) and 28% to LKR 853 Mn (FY23: LKR 664 Mn, 9MFY24: LKR 662 Mn) respectively. However, the key driving factor of rise in profit was mirrored in the growth in interest income in FY23 which recorded an increase of 109% to LKR 5,392 Mn (9MFY24: LKR 4,742 Mn).

Financial Risk

Credit Risk The gross NPL of AAF has increased to 24.9% in 9MFY24 from ~16% in FY23. From FY23 onwards it has exceeded the industry level. These high NPLs are driven by their legacy portfolio where majority has been provided for. But gold backed portfolio minimizes the credit losses due to high marketability of gold.

Market Risk In terms of assets, the cash and cash equivalents and savings accounts with banks have increased in 9MFY24 by 4% to LKR 621 Mn and 42% to LKR 2,059 Mn respectively from FY23. The investments in re-repo agreements have declined by 16% to LKR 2,042 Mn. The advances and lease portfolio has contracted by 15% to LKR 17,012 Mn.

Liquidity And Funding The highest funding is from customer deposits which accounts for 64%. In 9MFY24 (FY23: 61%). This has shrunk by 7% to LKR 12,373 Mn in 9MFY24 from FY23. The Company liquidity position, total liquid assets increased by 90% in FY23 to LKR 4,505 Mn and it is well above the required amount of LKR 1,100 Mn.

Capitalization The Capital Adequacy Ratio was 25.07% as of 9MFY24 and 27.43% in FY23 which is well above the requirement.



Lanka Rating Agency

Asia Asset Finance PLC
Listed

Dec-23	Sep-23	Jun-23	Mar-23	Mar-22	Mar-21
9M	6M	3M	12M	12M	12M

A BALANCE SHEET

1 Total Finance-net	14,199	16,485	15,158	18,489	15,180	11,343
2 Investments	2,367	4,353	2,678	2,769	1,349	1,031
3 Other Earning Assets	2,100	796	3,862	1,886	1,276	870
4 Non-Earning Assets	1,336	888	1,028	879	904	1,038
5 Non-Performing Finances-net	2,813	2,912	3,121	989	633	1,067
Total Assets	22,816	25,434	25,848	25,013	19,342	15,350
6 Funding	19,453	22,049	22,532	21,726	16,473	13,058
7 Other Liabilities	132	247	250	274	113	70
Total Liabilities	19,585	22,296	22,782	22,000	16,586	13,128
Equity	3,231	3,138	3,066	3,011	2,756	2,222

B INCOME STATEMENT

1 Mark Up Earned	4,742	3,271	1,636	5,392	2,576	2,725
2 Mark Up Expensed	(3,402)	(2,409)	(1,229)	(3,651)	(1,324)	(1,462)
3 Non Mark Up Income	311	187	87	615	607	230
Total Income	1,651	1,050	494	2,355	1,858	1,492
4 Non-Mark Up Expenses	(961)	(623)	(286)	(1,397)	(1,127)	(978)
5 Provisions/Write offs/Reversals	(351)	(231)	(110)	(556)	(493)	(383)
Pre-Tax Profit	338	195	98	402	239	132
6 Taxes on Financial Services	(60)	(33)	(17)	(43)	(37)	(45)
Profit Before Income Taxes	278	162	81	360	202	87
7 Income Taxes	(54)	(35)	(26)	(64)	(84)	(42)
Profit After Tax	224	127	55	295	119	45

C RATIO ANALYSIS

1 PERFORMANCE

a Non-Mark Up Expenses / Total Income	58.2%	59.4%	57.8%	59.3%	60.6%	65.5%
b ROE	9.6%	8.3%	7.3%	10.2%	4.8%	2.1%

2 CREDIT RISK

a Gross Finances (Total Finance-net + Non-Performing Advances + Non-Performing Debt Instruments) / Funding	97.2%	96.7%	89.2%	97.6%	105.3%	107.5%
b Accumulated Provisions / Non-Performing Advances	40.2%	39.9%	36.9%	63.5%	70.8%	60.3%

3 FUNDING & LIQUIDITY

a Liquid Assets / Funding	24.6%	22.9%	29.2%	20.7%	14.5%	12.7%
b Borrowings from Banks and Other Financial Institutions / Funding	30.2%	27.5%	26.1%	27.9%	33.4%	36.8%

4 MARKET RISK

a Investments / Equity	73.3%	138.7%	87.4%	92.0%	49.0%	46.4%
b (Equity Investments + Related Party) / Equity	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

5 CAPITALIZATION

a Equity / Total Assets (D+E+F)	14.2%	12.3%	11.9%	12.0%	14.2%	14.5%
b Capital formation rate (Profit After Tax - Cash Dividend) / Equity	8.6%	8.5%	7.3%	9.7%	5.3%	2.1%

Notes

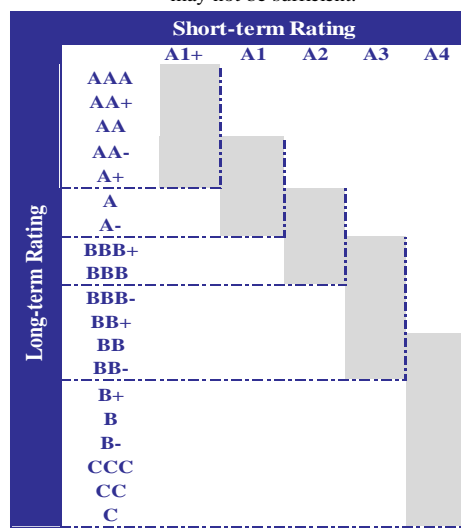


Credit Rating

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.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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.
AA-	
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.
A-	
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.
BBB-	
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.
BB-	
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.
B-	
CCC	
CC	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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating 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 surveil 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

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Regulatory and Supplementary Disclosure

(Rules applicable to Credit Rating Agencies, No. 19 of 2021 - issued on 15th March 2022)

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

(14) All information contained herein is considered proprietary by LRA. Hence, none of the information in this document can be copied or, otherwise reproduced, stored or disseminated in whole or in part in any form or by any means whatsoever by any person without LRA's prior written consent.