Lanka Rating Agency

# Rating Report

## Lanka Credit and Business Finance PLC

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**Rating History**

| Dissemination Date | Long Term Rating | Outlook | Action | Rating Watch |
|---|---|---|---|---|
| 11-Mar-2025 | BB- | Stable | Upgrade | - |
| 06-Jun-2023 | B+ | Positive | Initial | Yes |

**Rating Rationale and Key Rating Drivers**

After a period of economic and political turbulence, Sri Lanka's economy demonstrated a notable recovery in 2024. The first nine months of FY25 saw GDP growth of roughly 5.2%, fueled by strong performance in agriculture and services sector. Economic indicators improved significantly, including currency stabilization, single-digit policy rates, and a sharp decline in inflation (-4.0% YoY in January 2025). This positive shift has lowered both country and systemic risk, benefiting Sri Lankan Licensed Finance Companies (LFCs). The LFC sector experienced asset growth of ~13.9% and a substantial improvement in asset quality with the gross NPL ratio falling to about 11.3% in 9MFY25 (FY24: ~14.7%). This was due to increased size of lending portfolio and better repayment capacity of the borrowers. CBSL's master plan for consolidation of NBFIs Phase-II has been revised and is underway now.
Lanka Credit & Business Finance PLC (“LCBF” or “the Company”) remains a small player in a very competitive LFC sector in Sri Lanka. It offers various financial services, while having primary focus on term loans, lease and gold loans. The Company has identified agriculture and tourism sectors for its future growth. LCBF has plans of further expansion by establishing branch network in the rural areas of the island to increase its foothold in agrarian communities. LCBF intends to tap into the microfinance segment by providing bulk loans to the cooperative societies. The ownership structure holds a prevalent role in the Company's stability. The parent company and major shareholder, Lanka Credit and Business Limited ("LCBL"), provides support in terms of capital infusion and management expertise. LCBF potential merger with Lanka Cooperative Leasing Company ("LCLC") was called off. LCBF's net interest income saw an increase of ~27% in 9MFY25 on YoY basis due to better asset yields and lower cost of funds. LCBF's profitability remains modest as it posted a net profit of LKR ~138mn in 9MFY25 (FY24: LKR ~111mn). LCBF is expected to maintain adequate liquidity with cushion in unutilized borrowing lines. However, the Gross NPLs have been oscillating above the industry average for the last four years despite having a relatively small lending portfolio. During 9MFY25 Gross NPLs of the Company were recorded at ~15.3% whereas the industry average was ~11.3%. The NPL ratio for the fresh disbursements during the last one year is ~4.5%. The Company has net capital base of LKR~3bn, meeting the minimum capital requirement. The Company as of 9MFY25, has maintained a score above the threshold requirement under the CBSL's revised master plan for consolidation of the sector.

The rating is dependent on the management's ability to navigate through low-interest rate environment and insulate the asset quality from further deterioration while maintaining the growth momentum. Reducing non-performing loans (NPLs) in line with the industry is important. Any pronounced increase in credit risk, resulting in higher provisioning expenses, could negatively affect the rating.

**Disclosure**

| | |
|---|---|
| **Name of Rated Entity** | Lanka Credit and Business 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(Feb-25) |
| **Rating Analysts** | Imran Iqbal \| imran@lra.com.lk \| +94 114 500099 |

## Profile

**Structure** Lanka Credit & Business Finance PLC ("LCBF" or "the Company") was incorporated on 5th September 2016 as a Public Limited Liability Company. Incorporated and domiciled in Sri Lanka under the Companies Act No. 07 of 2007. The company is approved under the Finance Business Act No. 42 of 2011 and is listed in the Colombo Stock Exchange

**Background** Lanka Credit and Business Finance PLC (formerly known as City Finance Corporation Limited). was restructured as a result of an investment made by Lanka Credit and Business Limited under the guidance of the Central Bank of Sri Lanka in May 2018. The Company's ultimate parent and controlling party is Lanka Credit and Business Limited,

**Operations** The Company provides a comprehensive range of financial services, including accepting deposits and offering credit facilities such as finance leases, hire purchase, vehicle loan facilities, mortgage loans, gold loans, revolving loans, business/personal loans, and other credit facilities.

## Ownership

**Ownership Structure** The major shareholding vests with Lanka Credit and Business Limited ("LCBL") owning 72.1% as at 9MFY25. The second largest shareholder is Nation Lanka Finance Plc followed by Mr. Kapila Indika Weerasinghe.

**Stability** The Nanayakkara family owns ~24% of LCBL (the parent company). The sponsor provide support in the form of equity injection in the business through LCBL.

**Business Acumen** LCBL does not have any operations other than management of investment in LCBF. The shareholders of LCBL are well reputed businessmen with other profitable ventures as well.

**Financial Strength** The financial strength of the Company is derived from its shareholders, who are well-known for their business investments.

## Governance

**Board Structure** The LCBF board consists of nine (9) members out of which three (3) are Non-Executive/Independent Directors and includes the Chairman. The board also has five (5) Non-Executive/Non-Independent Directors and one (1) Executive Director, who is the Chief Executive Officer ("CEO") of the Company.

**Members' Profile** The Board comprises individuals with knowledge, expertise, and experience in various fields, including IT, law, finance, and government services. Mr. Dushmantha Thotawatta serves as the Chairman of the Company and was appointed to the Board in 2020.

**Board Effectiveness** LCBF operates with five (5) board sub-committees, namely Board Audit Committee ("BAC"), Board Human Resource and Remuneration Committee ("BHRC"), Board Integrated Risk Management Committee ("BIRMC"), Credit Committee ("CC") and Board Related Party Transactions Review Committee ("BRPTRC").

**Financial Transparency** E&Y Chartered Accountants of Sri Lanka has provided an unqualified audit opinion on the financial statements for FY24.

## Management

**Organizational Structure** The Company has a well-defined organizational structure with thirteen (13) divisions. The final authority lies with the CEO who reports to the Board of Directors. In addition, the board Integrated risk management committee, board audit committee, and the company secretary report directly to the board.

**Management Team** The management team is steered by Mr. Kandegoda Gamage, who functions as the CEO/ Executive Director and has the relevant qualifications and experience.

**Effectiveness** The Company has formed seven (7) management committees that assist the Company to effectively carry out its operations.

**MIS** The Company has a centralized IT function. The IT department directly reports to the CEO. It uses "eFinancials" as the core system, which is provided by Scienter Pte Ltd, to handle basic customer information, loans, leasing, hire purchase, gold loan, and fixed deposit information.

**Risk Management Framework** LCBF has established a dedicated risk management department, separate from the finance department which overlooks policy implementation for integrated and operational risk management.

## Business Risk

**Industry Dynamics** There are 33 Licensed Finance Companies ("LFC") in Sri Lanka, out of which, 27 are listed on the CSE. The sector profitability of the LFC sector improved by ~64% to LKR~51.5bn in FY24 compared to FY23 which was LKR~33.2bn (9MFY25: LKR~43.1bn). The deposits of the LFC sector increased by ~8.8% in FY24 to LKR~987bn while it was at LKR~907.2bn in FY23 (9MFY25: LKR~1,056.9bn). However, total borrowings of the sector depicted a decline by ~11.4% in FY24 to LKR~248.5bn from LKR~281.2bn in FY23 (9MFY25: LKR~305.3bn). Total loans and advances of the sector have increased by ~4.7% to LKR~1,214.7bn in FY24 from LKR~1,159.9bn in FY23 (9MFY25: 1,430.2bn). The total asset base of the LFC sector stood at LKR~1,630.3bn and LKR~1,760.7bn as at FY23 and FY24 respectively (9MFY25: LKR~1,930.7bn).

**Relative Position** The Company represents 0.68% of the equity in the LFC industry as at 9MFY25. Moreover, the Company asset base contributes to 0.44% of the industry assets during 9MFY25.

**Revenues** The revenue clocked in at LKR ~1.03bn in 9MFY25 and remained the same when compared to 9MFY24. Net Interest Income for 9MFY25 was LKR ~576mn which has shown a growth of ~27% from 9MFY24. This improvement can be attributable to expansion of the Company's lending book. The Company's product portfolio is predominantly focused on term loans, leases, gold loans which collectively amount for ~85.3% of the total lending portfolio in 9MFY25. During 9MFY25 interest income from term loans contributed ~65% followed by interest income from leasing which accounted for 19% of the total interest income. The trend in increase in revenue is expected to continue as opening of new branches is in the pipeline and penetration in cooperative sector is on the cards. However, impact on revenue from fall in policy rates remains pronounced.

**Performance** LCBF profitability improved by 48% in 9MFY25 to LKR ~138mn from LKR ~93mn in 9MFY24. This growth can be attributable to a decrease in interest expense of ~23% from LKR 469mn in 9MFY24 to LKR 360mn in 9MFY25, an increase in fee and commission income of 40% and 38% reduction in impairment charge during 9MFY25 when compared to 9MFY24. The asset base of the Company has improved by ~19.4% to clock in at LKR ~8bn as at 9MFY25 (9MFY24: LKR ~ 6.6bn). The total advances have increased by ~58% from 9MFY24 to 9MFY25. The Company's Return on Asset ("ROA") and Return on Equity ("ROE") is recorded at ~2.75% and ~4.52% as at 9MFY25 respectively.

**Sustainability** LCBF strategic direction is focusing on realigning the Company with major customer segments of leasing, SME and microfinance through cooperative societies. Sectors in which the Company expects potential growth are tourism and agriculture. In order to differentiate itself from competitors the Company plans to improve its agriculture sector products and green products.

## Financial Risk

**Credit Risk** The Company's gross NPL is recorded at ~15.3% in 9MFY25 (FY24: ~23%), while the net NPL was recorded at ~6% (FY24: ~12%) which is higher than the industry average due to the nature of the product being offered by the Company.

**Market Risk** A negative growth of ~43% has been witnessed in assets subject to market risk in 9MFY25 and make up ~6.5% of the total assets of the Company. Investment in fixed deposit and commercial papers have a short-term maturity.

**Liquidity And Funding** LCBF's majority funds are from customer deposits and represent ~87% of the total funding in 9MFY25. The deposit base of the Company has significantly risen in 9MFY25 by ~28% to LKR ~3.05bn (9MFY25: LKR ~2.3bn) due to deposit mobilization from cooperative societies. The Company's top 20 depositor come out to be 42% of the total deposit as at 9MFY25 which is considered to be high.

**Capitalization** The Total Capital Adequacy Ratio stood at 45.15% in FY23 and 42.07% in FY24, (9MFY25 :~36.7%) while Tier 1 was also 45.15% in FY23 and 42.07% in FY24 (9MFY25:~36.6%). Although CAR ratios are well above the CBSL stipulations, but it also reflect the unutilized potential of capital invested.

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| LANKA CREDIT AND BUSINESS FINANCE PLC | Dec-24 | Mar-24 | Mar-23 | Mar-22 |
|---|---|---|---|---|
| # | 9M | 12M | 12M | 12M |
| **A BALANCE SHEET** | | | | |
| 1 Total Finance-net | 6,562 | 4,435 | 3,893 | 3,425 |
| 2 Investments | 168 | 1,087 | 628 | 20 |
| 3 Other Earning Assets | 254 | 167 | 150 | 205 |
| 4 Non-Earning Assets | 474 | 599 | 518 | 358 |
| 5 Non-Performing Finances-net | 455 | 726 | 689 | 349 |
| **Total Assets** | 7,912 | 7,013 | 5,877 | 4,357 |
| 6 Funding | 4,686 | 3,953 | 3,024 | 1,625 |
| 7 Other Liabilities | 274 | 141 | 57 | 50 |
| **Total Liabilities** | 4,959 | 4,094 | 3,081 | 1,676 |
| **Equity** | 3,058 | 2,919 | 2,796 | 2,681 |
| **B INCOME STATEMENT** | | | | |
| 1 Mark Up Earned | 937 | 1,202 | 1,032 | 504 |
| 2 Mark Up Expensed | (361) | (620) | (427) | (105) |
| 3 Non Mark Up Income | 92 | 166 | 72 | 37 |
| **Total Income** | 669 | 749 | 677 | 437 |
| 4 Non-Mark Up Expenses | (365) | (416) | (325) | (218) |
| 5 Provisions/Write offs/Reversals | (81) | (123) | (91) | 62 |
| **Pre-Tax Profit** | 222 | 210 | 260 | 280 |
| 6 Taxes on Financial Services | (24) | (72) | (48) | (41) |
| **Profit Before Income Taxes** | 198 | 138 | 213 | 239 |
| 7 Income Taxes | (60) | (26) | (50) | (141) |
| **Profit After Tax** | 138 | 111 | 163 | 98 |
| **C RATIO ANALYSIS** | | | | |
| **1 PERFORMANCE** | | | | |
| a Non-Mark Up Expenses / Total Income | 54.6% | 55.6% | 48.1% | 50.0% |
| b ROE | 6.2% | 3.9% | 5.9% | 3.6% |
| **2 CREDIT RISK** | | | | |
| a Gross Finances (Total Finance-net + Non-Performing Advances + Non-Performing Debt Instruments) / Funding | 163.0% | 141.4% | 161.8% | 245.9% |
| b Accumulated Provisions / Non-Performing Advances | 57.8% | 37.1% | 31.0% | 39.0% |
| **3 FUNDING & LIQUIDITY** | | | | |
| a Liquid Assets / Funding | 22.4% | 28.7% | 33.2% | 61.3% |
| b Borrowings from Banks and Other Financial Institutes / Funding | 12.3% | 15.3% | 18.7% | 36.1% |
| **4 MARKET RISK** | | | | |
| a Investments / Equity | 5.5% | 37.2% | 22.5% | 0.7% |
| b (Equity Investments + Related Party) / Equity | 0.0% | 0.5% | 0.5% | 0.7% |
| **5 CAPITALIZATION** | | | | |
| a Equity / Total Assets (D+E+F) | 38.6% | 41.6% | 47.6% | 61.5% |
| b Capital formation rate (Profit After Tax - Cash Dividend ) / Equity | 6.3% | 4.0% | 4.3% | 3.6% |

## Credit Rating

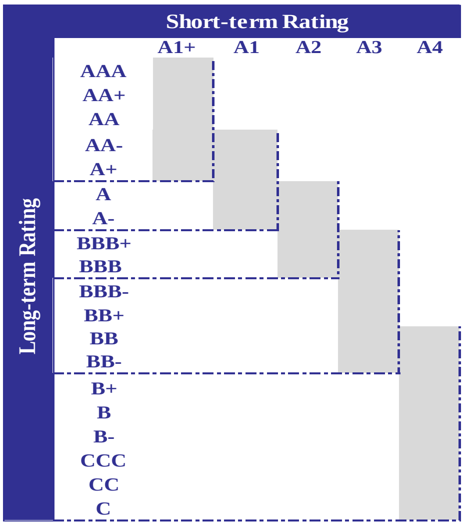
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

### 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+<br>AA<br>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+<br>A<br>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+<br>BBB<br>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+<br>BB<br>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+<br>B<br>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<br>CC<br>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

## 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**