Lanka Rating Agency

Rating Report

Sarvodaya Development Finance PLC

Report Contents

Rating History

Dissemination Date	Long Term Rating	Outlook	Action	Rating Watch
11-Apr-2025	BB+	Stable	Upgrade	-
02-Oct-2023	BB	Stable	Maintain	-
21-Sep-2022	BB	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Sri Lankan economy has witnessed a turnaround during 2024 after two years of economic and political uncertainty. With a GDP growth of ~5.2% in 9MFY25, other economic indicators have also improved. Agriculture and services sector have been the main drivers that have bolstered this growth. As the currency tends to stabilize and the policy rates in the single digit, inflation has also witnessed a significant drop (-4.0% YoY in January 2025). These economic factors have brought about a reduction in country as well as systematic risk. This economic recovery has, in turn, been beneficial for the Licensed Finance Companies (LFCs) in Sri Lanka. Total assets of the LFC sector grew by ~13.9% at the end of 9MFY25 while asset quality improved (Gross NPL ratio 9MFY25: ~11.3%; 9MFY24: ~18%) due to growing loans and advances and better repayment capacity of borrowers.

Sarvodaya Development Finance ("SDF" or the Company) is a small player in the LFC sector with strong presence and connectivity in the rural community. The rating reflects substantial growth in the Company's loan portfolio, improved profitability and strong liquidity position. The Company has managed to increase its MSME, lease and gold loan portfolio. The Company has high exposure to the agriculture and transportation segments with a large leasing portfolio of ~44% that focuses on agriculture-based leasing. The Company has entered into buy-back agreements with distributors to reduce the default risk on its leasing portfolio. The Company's net interest income has witnessed an increase of ~51% in 9MFY25 on YoY basis due to higher asset yields and comparatively lower funding cost. The Company clocked in a net profit of LKR~339mn in 9MFY25 (FY24: LKR~250mn). Liquidity is anticipated to improve as tranches from European Development Finance Institutions amounting to USD~3mn have already been realized. Further loans from international loans are in the pipeline that will diversify funding base. The limiting factor in the Company's rating is its small size and modest capital base. The Company has managed to maintain the gross and net non-performing loans (NPLs) below the industry average even though its target market constitutes economically vulnerable segment of the population. SDF's CAR stands at 19.7% with a net capital base of LKR~3.9bn as at 9MFY25. Going forward, successful credit management will remain critical for the Company.

The rating is dependent upon the Company's ability to preserve its unique accessibility to the rural segment in the island. Sustaining its growth momentum while improving margins will be key for the Company. The rating will rely on the successful execution of the Company's strategy to grow its asset base while preserving the asset quality. Any notable increase in credit risk, resulting in higher provisioning expenses, could negatively affect the rating.

Disclosure

Name of Rated Entity	Sarvodaya Development 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	Gayani Randima Ariyawansa | gayani@lra.com.lk | +94 114 500099

Profile

Structure Sarvodaya Development Finance PLC ("SDF" or "the Company") is a public limited liability company, incorporated in 2010, under the Companies Act No. 07 of 2007 and the Finance Business Act No. 42 of 2011. SDF was listed on the Colombo Stock Exchange ("CSE") in December 2021.

Background The Company was incorporated as Deshodaya Development Finance Company Limited in 2010 and assumed its current name in 2015.

Operations The principal business activities include acceptance of deposits, granting micro finance loans, SME loans, leasing, housing loans, business loans, pawning and other credit facilities, digital financial services and other value-added services. The Company has 56 branches, of which more than 90% are situated outside the Western Province. SDF is connected to 5,400 societies (through Sarvodaya Movement) with more than 800,000 members.

Ownership

Ownership Structure The largest share of the company is owned by Sarvodaya Economic Enterprises Development Services (GTE) Ltd ("SEEDS"), with an ownership of ~36.1%, while the Sarvodaya Movement collectively owns ~55% of the Company. Janashakthi Capital Limited, Senthilverl Holdings (Pvt) Ltd and Gentosha Media Consulting Inc. owns ~10.8%, ~12.1% and ~9% respectively.

Stability SEEDS was established in 1986 as the economic arm of the Sarvodaya Movement. The ownership of SEEDS has not gone through a major change, since it has been able to maintain its shareholding, post listing in CSE.

Business Acumen SEEDS is engaged in economic development of rural communities through providing training in business development skills and financial services.

Financial Strength The Sarvodaya Movement has multiple companies and independent units which operates under it. The Company does not have a written financial guarantee from the parent entity or other shareholders.

Governance

Board Structure The Board of Directors comprises of seven non-executive Directors, of which four are independent and three are non-independent.

Members' Profile The Board members have diverse expertise in banking, sales, marketing, IT, and consulting. They are well qualified in their respective domains along with decades of experience. The Chairman, Mr. Channa De Silva has held senior management positions in many reputed firms, including financial institutions and banks.

Board Effectiveness The Company has formed five board sub-committees, namely, i) Board Integrated Risk Management Committee ("BIRMC"), ii) Board Audit Committee ("BAC"), iii) Board Nomination and Governance Committee ("BRNC"), iv) Related Party Transaction Review Committee ("RPTRC"), v) Board Credit Committee ("BCC"), vi) Board Remuneration Committee

Financial Transparency The external auditors of the Company, Ernst & Young, issued an unqualified audit opinion pertaining to annual financial statements for FY24.

Management

Organizational Structure The Company has 15 separate divisions to carry out its operations. The Compliance Department and the Risk Departments report to the BIRMC, while the Internal Audit Department reports to the BAC.

Management Team The management team is headed by the Chief Executive Officer ("CEO"), Mr. Nilantha Jayanetti. The CEO has extensive knowledge in business management and strategic leadership and has experience in the banking and financial sectors.

Effectiveness SDF has formed five management committees, namely, i) Assets and Liability Management Committee ("ALCO"), ii) Management Credit Committee ("MCC"), iii) IT Steering Committee ("ITSC"), iv) Management Committee ("MC"), v) Product Development Committee ("PDC"), vi) Sustainability Committee ("SC"), vii) Information Security Committee ("ISC"), viii) Management Operation Risk Management Committee ("MORMC").

MIS The main ERP system of the Company is the eFinancials system, provided by Scienter Technologies (Pte) Ltd. The Company is also connected to the Lanka Pay CEFT network, Shared ATM Switch ("SAS") and Common ATM Switch ("CAS").

Risk Management Framework The BAC has the responsibility to ensure the integrity of the financial reporting and the effectiveness of the internal control systems. Risk reports are submitted to the BIRMC for each type of risk identified with a rectification plan. Heads of Departments have the responsibility to identify and focus on potential risks in their respective areas of operations.

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 remains a small player in the industry, as it accounts for ~1.04% of the assets in the sector as at 9MFY25 and its deposits as a percentage of the total sector deposit stood at ~0.85% in 9MFY25.

Revenues The Company's interest income of the Company increased by ~28.3% in 9MFY25 to LKR~2.9bn from LKR~2.3bn. Interest expense of the Company reduced by ~0.5% in 9MFY25 to LKR~990.9mn from LKR~996.2mn in 9MFY24 (FY24:LKR~3.1bn | FY23:LKR~2.5bn). This can be attributable to growth in gross loan and lease portfolio due to improvement in the economy on the macro level, despite the reduction in the lending rates in line with the policy rates.

Performance The Profit After Tax ("PAT") of the Company recorded a significant growth in 9MFY25 of ~129.8% to LKR~339.4mn from LKR~147.7mn in 9MFY24 (FY24: LKR~249.6mn | LKR~221.6mn). This improvement points to rise in net interest income as a result of higher asset yields compared to lower funding costs. ROE improved to 7.1%in FY24 (9FY25: 12.1%) from 6.6% in FY23. ROA remained low at 1.9% for both FY24 (9MFY25:2.6) and FY23.

Sustainability The Company intends to strengthen customer reach and accessibility by strategically growing the branch and ATM network to provide better financial access, especially to community-level businesses and economically active groups. SDF plans to expand market opportunities for MSMEs by fostering entrepreneurship among the youth and women associated with rural areas of the island.

Financial Risk

Credit Risk The Company has been able to improve its NPLs since FY20. However, it increased drastically in FY23 to ~18.09% and as a result of the dire economic condition of the country, however it remained less than industry averages. NPL recorded at ~10.77% and ~13.7% as at 6MFY25 and FY24. SDF has a granular customer base as the top 20 advances account for ONLY ~2.2% of the total advances as at 6MFY25 (FY24:2.9%).

Market Risk The Company increased its investments by ~25.8% in FY24 which saw a decreased of ~9.3% in 6MFY25. It increased its investment in government securities in FY24 by ~34.0% to LKR~772mn compared to LKR~576mn in FY23. Investments in government securities constituted ~73.3% of the total investments as at 6MFY25.

Liquidity And Funding The reliance on customer deposits decreased from ~21.0% in FY23 to ~17.4% in 6MFY25. Bank and other borrowings have dropped from ~99.3% in FY23 to ~58.8% in 6MFY24. Liquidity is anticipated to improve as tranches from European Development Finance Institutions amounting to USD~3mn have already been realized. Further loans from international loans are in the pipeline that will diversify funding base.

Capitalization The Company's CAR reduced to ~22.29% as of 6MFY25 compared to ~26.00% as of FY24 (FY23:~34.01%) against a statutory requirement of 12.50%. Tier-1 Capital Ratio of the Company stood at ~22.16% as of 6MFY25 and ~25.84% as of FY24.

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Sarvodaya Development Finance PLC	Sep-24	Mar-24	Mar-23	Mar-22
#	6M	12M	12M	12M
A BALANCE SHEET				
1 Total Finance-net	14,412	11,455	8,272	8,558
2 Investments	924	1,019	810	767
3 Other Earning Assets	1,088	494	604	42
4 Non-Earning Assets	783	810	476	487
5 Non-Performing Finances-net	1,044	1,119	1,509	1,321
Total Assets	18,250	14,898	11,670	11,174
6 Funding	13,769	10,700	7,821	7,199
7 Other Liabilities	695	627	399	670
Total Liabilities	14,464	11,327	8,221	7,870
Equity	3,786	3,571	3,449	3,305
B INCOME STATEMENT				
1 Mark Up Earned	1,876	3,102	2,461	1,822
2 Mark Up Expensed	(625)	(1,322)	(1,222)	(562)
3 Non Mark Up Income	115	210	124	96
Total Income	1,365	1,990	1,363	1,357
4 Non-Mark Up Expenses	(631)	(1,081)	(867)	(800)
5 Provisions/Write offs/Reversals	(173)	(318)	(51)	(181)
Pre-Tax Profit	562	591	446	375
6 Taxes on Financial Services	(150)	(182)	(146)	-
Profit Before Income Taxes	412	409	300	375
7 Income Taxes	(196)	(160)	(78)	(160)
Profit After Tax	216	250	222	215
C RATIO ANALYSIS				
1 PERFORMANCE				
a Non-Mark Up Expenses / Total Income	46.2%	54.3%	63.6%	59.0%
b ROE	11.7%	7.1%	6.6%	7.9%
2 CREDIT RISK				
a Gross Finances (Total Finance-net + Non-Performing Advances + Non-Performing Debt Instruments) / Funding	117.3%	124.0%	131.1%	144.9%
b Accumulated Provisions / Non-Performing Advances	39.9%	38.4%	23.8%	29.4%
3 FUNDING & LIQUIDITY				
a Liquid Assets / Funding	13.8%	12.8%	15.9%	8.7%
b Borrowings from Banks and Other Financial Institutes / Funding	34.7%	28.1%	19.3%	32.2%
4 MARKET RISK				
a Investments / Equity	24.4%	28.5%	23.5%	23.2%
b (Equity Investments + Related Party) / Equity	0.0%	0.0%	0.0%	0.0%
5 CAPITALIZATION				
a Equity / Total Assets (D+E+F)	20.7%	24.0%	29.6%	29.6%
b Capital formation rate (Profit After Tax - Cash Dividend) / Equity	12.1%	4.0%	4.4%	4.2%

Credit Rating

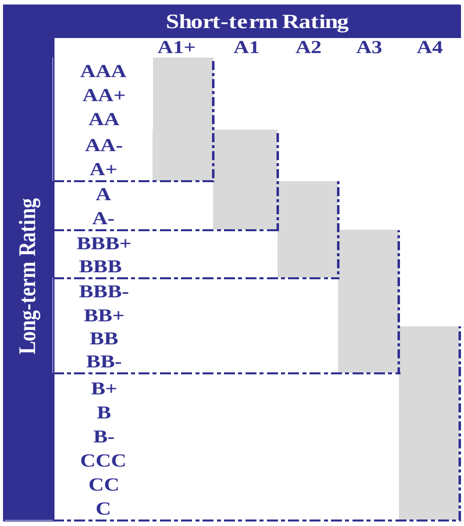
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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