Lanka Rating Agency

Rating Report

Regional Development Bank

Report Contents

Rating History

Dissemination Date	Long Term Rating	Outlook	Action	Rating Watch
02-May-2025	BBB+	Stable	Maintain	-
17-Jan-2024	BBB+	Stable	Initial	-

Rating Rationale and Key Rating Drivers

RDB is a state-owned Licensed Specialized Bank (LSB) in Sri Lanka that operates with a focus on economic development by providing financial assistance to Microfinance Institutions and Small and Medium Enterprises. The Bank provides loans across various sectors, including industry, commercial, agriculture, and individual segments. Overall economic conditions have improved in Sri Lanka resulting in relatively better performance of financial institutions in the country including LSBs. The rating reflects the Regional Development Bank's ("RDB" or "the Bank") sovereign ownership, adequate performance and its exposure to economically vulnerable segments based on its mandate. The interest rates in Sri Lanka have dropped to single digits. This led to increased Net interest income (NII) of the Bank to LKR~19.5bn in CY24 (CY23: LKR~16.9bn). The core spread has been improved to ~6.4% in CY24 as compared to ~3.5% in CY23 due to lagging repricing of assets. However, higher operating expenses and taxation has exerted pressure on the profitability. RDB's Profit After Tax (PAT) stood at LKR~1.3bn in CY24 (CY23: LKR~0.86bn), mainly driven by an impairment reversal of LKR~0.83bn. As of CY24, the Bank's Non-Performing Loans (NPLs) improved to ~10.76%, down from ~13.75% in CY23. This was based on growth in advances portfolio (~16.5%) and better recoveries.
RDB has altered its investment mix amidst changing interest rates towards fixed deposits to augment investment yield. The funding mix is dominated by short-term fixed and savings deposits, supported by a depositor base exceeding LKR~253.6bn. The average cost of funds ranges from ~6% to ~7%, with the Bank's core spread also falls between ~6% and ~7%. Despite a Capital Adequacy Ratio (CAR) of ~15.66% in CY24, Tier-1 capital has dipped to ~9.65%, but remains above the minimum regulatory requirement of ~8.5%. In terms of liquidity, the Bank meets the CBSL's statutory requirements; however, liquid assets accounted for only ~23% of the funding base in CY24, down from ~32% in CY23.
The Bank is in the process of filling certain key positions at senior level. Timely hiring and integration of these in the management team is important for sustainable performance, going forward.

The rating is dependent on improving the Bank's profitability indicators. Similarly, sustaining and strengthening its capital profile is crucial. Any adverse impact on capital and related regulatory ratios, leading to a regulatory breach, would have negative rating repercussions.

Disclosure

Name of Rated Entity	Regional Development Bank
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Financial Institution Rating(Aug-24)
Related Research	Sector Study | Commercial Bank (Dec-24)
Rating Analysts	Ruwanthi Sylva | ruwanthi@lra.com.lk | +94 114 500099

Profile

Structure Regional Development Bank (“RDB”, "the Bank") is a fully state-owned Licensed Specialized Bank (LSB) established under the Pradeshiya Sanwardana Bank Act No. 41 of 2008, located at No. 933, Kandy Road, Wedamulla, Kelaniya.

Background In 1985, ~17 banks were founded at the district level categorized as Regional Rural Development Banks. In 1997, these banks were merged into ~6 provincial level Banks. This collective transformation in 2010 resulted in the establishment of a national-level development bank known as the Pradeshiya Sanwardana Bank (Regional Development Bank).

Operations RDB focuses on accessible financial services for lower-income segments and has been recognized for its services. The Bank supports economic development in Sri Lanka by providing financial assistance to Micro Finance Institutions and SMEs across agriculture, industry, and women empowerment. As of CY24, it operates 272 service points in 19 districts with over 2,615 employees.

Ownership

Ownership Structure RDB is 100% state-owned (directly and indirectly) with the Government of Sri Lanka having a stake of ~91.21% and three state banks (Bank of Ceylon, Peoples Bank, and National Savings Bank) each owning ~2.93%.

Stability The Bank’s ownership has remained stable, with Government of Sri Lanka maintaining its ownership along with the other three major banks.

Business Acumen The Government of Sri Lanka provides strategic insights to RDB, represented on the Board of Directors by the Deputy Secretary to the Treasury and deputies from Bank of Ceylon, Peoples Bank, and National Savings Bank. This ensures vital industry expertise in governance and decision-making.

Financial Strength The Government of Sri Lanka supported RDB by injecting capital to improve its Capital Adequacy Ratio and guaranteed an LKR~15bn loan from the Asian Development Bank. This indicates that the Government's commitment to provides support to the Bank, where needed.

Governance

Board Structure The Bank's Board has 8 Non-Executive Directors, including 7 Independent Directors. The Secretary to the Treasury nominates the Chairman and directors. Mr. D.A.P. Abeysekara is the sole Nominee Director from the Ministry of Finance.

Members’ Profile Lasantha Fernando became RDB's 9th Chairman on November 1, 2024, bringing ~35 years of banking experience, including a role at Hatton National Bank. He holds a Diploma in Bank Management, is a Fellow of the Institute of Bankers, and has an MBA from the University of Colombo. The Board includes members with extensive expertise in banking, law, and finance.

Board Effectiveness RDB has 5 Board subcommittees: Audit, IT, Integrated Risk Management, HR and Remuneration, and Nomination. The Integrated Risk Management Committee monitors compliance with risk policies, while the Bank emphasizes employee training and regular audits to ensure effective risk management.

Financial Transparency The National Audit Office issued an unqualified audit opinion on RDB's CY24 financial statements.

Management

Organizational Structure The Bank is headed by the General Manager/Chief Executive Officer (GM/CEO), various Deputy General Managers (DGMs) reporting directly to the GM. DGMs lead their respective departments. Key departments report to their respective board committees, ensuring clear accountability.

Management Team The management team is led by Acting GM/CEO Mr. E A D Janitha Priyashantha, who joined RDB on June 27, 2022, bringing over ~30 years of banking and finance experience. The Bank is in the process of filling several key senior-level positions. Timely recruitment and effective integration of these roles into the management team will be critical to ensuring sustainable performance.

Effectiveness The Bank has established 21 management committees, including the IT Steering Committee, Executive Credit Committee, and Human Resource Policy Committee, to effectively manage operations.

MIS The Bank uses the Intellect CBS Banking System and has disaster recovery sites at SLT and Dialog/Hutch. Transactions are processed through counters and ATMs. A mobile banking app is in development, alongside other digital projects like an Anti-Money Laundering system.

Risk Management Framework The Bank adopts a 3-line risk management framework, governed by the Board of Directors. The Risk Management Department, led by the Chief Risk Officer, focuses on credit, operational, and market risks. Credit risk is the most significant, managed by an annually reviewed policy. Currently, CRO position is vacant.

Business Risk

Industry Dynamics In Sri Lanka, there are 30 banks. These include 24 LCBs and 6 LSBs. As of CY24, total assets are LKR~22.2tn (up ~8.7%), with deposits at LKR~17.9tn (up ~8.1%) and advances at LKR~11.5tn (up ~ 4.15). Net interest income (NII) was reported at LKR~916.8bn, while profit after tax (PAT) for the sector was LKR~321.5bn. The Capital Adequacy Ratio stood at ~18.4% in CY24 as compared to CY23.

Relative Position As of 9MCY24, NSB leads the LSB sector in Sri Lanka, with RDB as the second-largest player, holding ~12.3% of total advances and ~13.6% of total assets.

Revenues In CY24, the Bank's gross income was LKR~39.6bn, down ~17% from LKR ~47.6bn in CY23, mainly due to ~18% decline in interest income to LKR ~37.9bn. Interest expenses fell ~37% to LKR ~18.4bn, resulting in Net Interest Income (NII) of LKR~19.5bn (up ~15.4%), with a core spread rising to ~6.4%.

Performance The Bank reported a net operating income of LKR~21.4bn in CY24 (CY23: LKR~15.7bn). However, the rise in operating expenses led to an operating profit of around LKR~6.2bn in CY24 (CY23: LKR~3.5bn). Profitability was notably impacted by VAT, SSCL, and income tax. RDB’s Profit After Tax (PAT) reached LKR~1.3bn in CY24, an increase from LKR~0.86bn in CY23, largely supported by an impairment reversal of LKR~0.83bn. The Bank’s cost of funds declined to ~6.5%, while Return on Assets (ROA) and Return on Equity (ROE) stood at around ~0.4% and ~7%, respectively.

Sustainability The Bank launched an Entrepreneur Development Program to support 15,000 new entrepreneurs with loans of LKR~1mn to LKR~10mn. It aims to develop tourism and industry sectors and has introduced a digital credit approval system. Training for 100 branch managers is in progress, and two new branches will expand the network into the northern region.

Financial Risk

Credit Risk RDB’s gross NPL ratio improved from ~13.75% in CY23 to ~10.76% in CY24, while net NPLs dropped from ~8.80% to ~6.25%. This was based on growth in advances portfolio (~16.5%) and better recoveries. Industry gross NPLs was reported at ~12.3% in CY24. The Stage 3 Impairment Coverage Ratio of the Bank has improved to ~41.9%.

Market Risk In CY24, total investments declined to approximately LKR~25.4bn from LKR~61.1bn in CY23. While investments in CY23 primarily composed of Government securities, the portfolio in CY24 mainly consisted of fixed deposits with financial institutions. This shift towards fixed deposits and repos reflects a strategic response to prevailing economic conditions.

Liquidity And Funding As of CY24, over ~78% of the Bank's funding comes from deposits, up from ~75% in CY23. Time deposits make up ~66% of total deposits, while savings deposits account for ~33%. The concentration among the top 20 depositors rose to ~12.8% in CY24 from ~11% in CY23 but remains largely granular in nature. In terms of liquidity, the Bank meets CBSL's statutory requirements. However, liquid assets accounted for only ~23% of the funding base in CY24, down from ~32% in CY23.

Capitalization In CY24, the Capital Adequacy Ratio (CAR) stood at ~15.66% well below than the industry average, while Tier-1 capital declined to around ~9.65%, remaining above the regulatory minimum of ~8.5%. The Bank's equity reached LKR ~18.6bn in CY24, a ~4% increase from LKR ~17.9bn in CY23.

LRA

Financials (Summary) in LKR mln

Lanka Rating Agency

Regional Development Bank Public Limited	Dec-24	Dec-23	Dec-22	Dec-21
LKR mln	12M	12M	12M	12M
A BALANCE SHEET				
1 Stage I | Advances - net	175,128	129,542	146,906	127,122
2 Stage II | Advances - net	36,733	46,060	37,045	30,012
3 Stage III | Advances (NPLs)	26,339	29,425	20,656	25,466
4 Stage III | Impairment Provision	(11,032)	(10,603)	(6,599)	(7,370)
5 Investments	23,716	60,479	11,487	4,814
6 Debt Instruments	1,662	624	624	624
7 Other Earning Assets	61,110	31,870	59,104	56,017
8 Non-Earning Assets	10,264	12,320	16,171	9,205
Total Assets	323,920	299,716	285,395	245,890
6 Deposits	253,664	226,080	210,301	187,752
7 Borrowings	37,509	47,147	48,283	32,245
8 Other Liabilities (Non-Interest Bearing)	14,359	8,625	10,584	10,499
Total Liabilities	305,532	281,852	269,169	230,496
Equity	18,388	17,866	16,226	15,393
B INCOME STATEMENT				
1 Mark Up Earned	37,922	46,233	35,273	23,545
2 Mark Up Expensed	(18,368)	(29,290)	(19,640)	(9,893)
3 Non Mark Up Income	1,630	1,354	929	947
Total Income	21,185	18,297	16,563	14,599
4 Non-Mark Up Expenses	(15,829)	(12,626)	(11,712)	(9,416)
5 Provisions/Write offs/Reversals	833	(2,163)	(2,852)	(3,257)
Pre-Tax Profit	6,189	3,508	1,998	1,927
6 Taxes on Financial Services	(2,979)	(2,325)	(1,639)	(1,151)
Profit Before Income Taxes	3,210	1,183	359	776
7 Taxes	(1,934)	(320)	990	(469)
Profit After Tax	1,275	864	1,350	306
C RATIO ANALYSIS				
1 Revenues				
Advances' Yield	13.5%	15.7%	12.9%	11.7%
Spread | Asset Yield - Cost of Funds	6.9%	6.6%	6.7%	6.7%
2 Performance				
Cost of Funds [Mark Up Expensed / Average (Deposits + Borrowings)]	6.5%	11.0%	8.2%	4.7%
ROE	7.0%	5.1%	8.5%	2.0%
3 Capital Adequacy				
Capital Adequacy Ratio	15.7%	17.3%	15.2%	14.3%
Net Stable Funding Ratio [Available Stable Funding / Required Stable Funding]	152.0%	174.0%	101.0%	127.0%
4 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	23.1%	31.6%	26.0%	25.3%
Demand & Saving Deposit Coverage Ratio	1.2	2.0	1.7	1.2
Top 20 Deposits / Deposits	12.8%	11.0%	7.4%	9.1%
5 Credit Risk				
Impaired Loan Ratio | [Stage III | Advances (NPLs) / Gross Advances]	10.8%	13.8%	9.6%	13.5%
Provision Coverage Ratio | [Impairment Provision / Stage III | Advances (NPLs)]	41.9%	36.0%	31.9%	28.9%

Scale – Credit Rating

Credit Rating

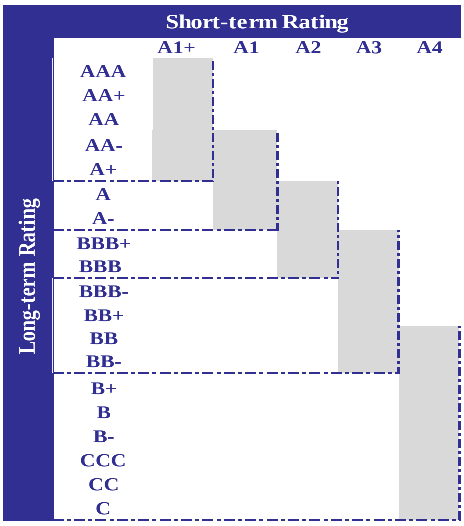
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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
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