Lanka Rating Agency

Rating Report

State Mortgage & Investment Bank

Report Contents

Rating History				
Dissemination Date	Long Term Rating	Outlook	Action	Rating Watch
20-Jun-2025	BBB	Stable	Maintain	Yes
20-Nov-2023	BBB	Stable	Initial	-

Rating Rationale and Key Rating Drivers

State Mortgage and Investment Bank (SMIB or The Bank) operates as a licensed specialized bank, wholly owned by the Government of Sri Lanka, implying strong linkage to the sovereign and potential state support. The Bank has an established operating history, although its presence in the sector remains limited, reflected by its share of ~4.4% and ~2.4%, in sector assets and deposits, respectively. The Bank's operational focus is primarily retail-oriented, with lending concentrated in personal loans, housing finance backed by Employee Provident Fund ("EPF") balances, and mortgage facilities. The Bank's core capital continues to fall short of the regulatory minimum requirement of LKR 7.5bn. To achieve compliance, a capital infusion of approximately LKR 1.7bn is deemed necessary. The Bank's management is exploring various options to meet capital requirements including potential amalgamation with another state-owned bank and capital injection by the Government. However, meaningful progress has not been made in this regard. The Bank seeks extension from CBSL for meeting regulatory capital requirement and a response is awaited.

The relatively low interest rates during CY24 have resulted in a decline in profitability indicators of the Bank, where Net Interest Margin ("NIM") moderated to ~3.8% in CY24 (CY23: ~1.0%) remaining below industry average of ~4.6%. The Bank posted a Profit After Tax of LKR 36mn in 3MCY25, sustaining its recovery following a PAT of LKR ~32mn in CY24. This reflects a gradual improvement from the loss of LKR 1bn reported in CY23. The Bank's asset quality remains under pressure, with the non-performing loan ("NPL") ratio rising to ~33.0% in CY24 and further to ~36.0% as of 3MCY25, significantly higher than the industry average of ~12.9%. NPL ratio of SMIB has historically remained elevated, largely driven by delinquencies within the EPF loan portfolio. Nonetheless, the risk is partially mitigated by The Bank's ability to recover through EPF balances at the end of each year. NPL ratio without EPF stood at ~17% in CY24 (CY23: ~14.0%). SMIB's CAR remains at a comfortable level, supported by low-risk assets such as EPF-backed and mortgage loans. As of CY24 Tier 1 and Total CAR were reported at ~19.3% (3MCY25: ~19.6%) and ~19.3% (3MCY25: ~17.9%), respectively. However, the CAR is expected to moderate as the Bank gradually shifts its lending focus away from zero-risk weighted EPF loans and diversifies its exposure. The "Rating Watch" signifies these developments and potential impact on the Bank's rating.

The rating is dependent on asset quality, profitability indicators, and the capitalization of the Bank. The Bank's ability to meet regulatory requirements or garner support from the Government will remain critical. Any weakening of profitability levels and/or deterioration in asset quality will have a negative effect on the rating. The Bank's ability to effectively realize operational and strategic synergies from the proposed amalgamation will be a key consideration for the rating and will be assessed upon completion of the transaction.

Disclosure	
Name of Rated Entity	State Mortgage & Investment 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	Gayani Randima Ariyawansa | gayani@lra.com.lk | +94 114 500099

Profile

Structure State Mortgage and Investment Bank ("SMIB" or "The Bank") is a Government-Owned Bank, established under State Mortgage and Investment Bank Law No. 13 of 1975. The Bank was recognized as a Licensed Specialized Bank ("LSB") and the license was issued by the Central Bank of Sri Lanka on April 27, 1998, vide Banking Act No. 30 of 1988.

Background The Bank was inaugurated as the Ceylon State Mortgage Bank ("CSMB") in 1931 vide Ordinance No. 16 of 1931. The Bank was formed by amalgamating the Ceylon State Mortgage Bank and the Agricultural and Industrial Credit Corporation established in 1943. The Bank commenced its operation on January 1, 1979.

Operations The Bank's principal operations consist of promoting housing, agricultural and industrial development finance and mobilization of deposits. Recently SMIB has diversified into other credit facilities such as vehicle loans and personal loans. SMIB operates 25 branches as of CY24, with a staff strength of 353.

Ownership

Ownership Structure 100% of shares owned by Government of Sri Lanka and all directors are appointed by the relevant line of Ministry vide State Mortgage and Investment Bank Law No. 13 of 1975.

Stability SMIB has proven history of receiving financial and managerial support from the Government of Sri Lanka ("GOSL"). The Bank's ownership has remained stable, with the Government maintaining 100% ownership.

Business Acumen Since the Bank comes directly under the purview of the Ministry of Finance, Economy, and Policy Development, SMIB stands to gain industry-specific knowledge from the GOSL.

Financial Strength The Bank has submitted a report to the Ministry of Finance regarding the current status of meeting the minimum regulatory capital requirements. A positive response from the Ministry is currently awaited. Furthermore, a financial due diligence process is underway in relation to the proposed amalgamation between SMIB and another state owned bank.

Governance

Board Structure SMIB's Board of Directors is appointed by the Ministry of Finance, Economy and Policy Development. The Bank has a Board of 6 Non-Executive directors out of which 5 independent directors.

Members' Profile The Chairman of the Bank, Mr. M. P. Kurugama has over 36 years of experience. He is an associate member of the Institute of Bankers of Sri Lanka (IBSL) and an alumnus of the Harvard Business School (USA). The remaining members of the Board holds decades of experience and qualifications in fields including legal and finance.

Board Effectiveness The Board has formed 4 board sub committees, namely, Board Integrated Risk Management Committee ("BIRMC"), Board Audit Committee ("BAC"), Board Nomination Committee ("BNC"), Board Human Resources and Remunerations Committee ("BHRRC").

Financial Transparency The external auditors of SMIB, the Auditor General, issued an unqualified audit opinion pertaining to financial statements for CY24.

Management

Organizational Structure The management of the Bank is overseen by the BoD through CEO and Board Committees. All departments of the Bank report to the CEO/GM, through respective DGMs.

Management Team The management team is headed by the CEO/GM, Mr. I.T. Asuramanna. He was appointed in July 2022 and has over 25 years of experience in finance. The CEO is supported by a large team of DGMs and AGMs.

Effectiveness The Bank has formed 6 management committees, namely, Executive Credit Committee ("ECC"), Asset Liability Management Committee ("ALCO"), Marketing Committee ("MC"), Product Development Committee ("PDC"), Recovery Committee ("RC"), Executive Integrated Risk Management Committee ("EIRMC").

MIS Due to its smaller scale, SMIB focuses on technology-driven outreach over branch expansion. It has completed its core banking system rollout, is partnering with a leading bank for ATM services along with enhancing its internet banking platform.

Risk Management Framework The Bank has a risk management framework based on the three lines of defense model. The BIRMC advises the Board of Directors on risk-related matters.

Business Risk

Industry Dynamics The banking sector consists of 30 banks, including 24 LCBs and 6 LSBs. As of CY24, the LSBs showed growth in assets, investments, and deposits compared to CY23. However, while profitability improved, quality of loans and advances declined relative to the previous year.

Relative Position SMIB, a small-sized LSB operating with only 25 branches, accounted for ~4.4% of the LSBs' advances and ~2.4% of their deposits as of CY24.

Revenues In CY24, the Bank's interest income declined YoY by ~18.6% to LKR~7.6bn (3MCY25: LKR~1.8bn | CY23: LKR~9.3bn), while interest expenses dropped more sharply by ~38.3% YoY to LKR~5.4bn (3MCY25: LKR~1.0bn | CY23:LKR~8.7bn). The contraction in both metrics reflects the lower interest rate environment, which compressed loan yields and simultaneously reduced the cost of funding.

Performance The Bank reported a turnaround in CY24, with PAT improving to LKR~32.0mn, compared to a loss of LKR~1.0bn in CY23 (3MCY25: LKR~36.0mn). The recovery was driven by stronger net interest income, higher fee-based income, improved investment gains, and enhanced operational efficiency. The cost of funds declined markedly to ~10.7% YoY (3MCY25: ~8.3% | CY23: ~17.2%), reflecting the impact of a lower interest rate environment. Consequently, key profitability metrics also improved, with ROA and ROE rising to ~0.6% and ~0.1%, respectively, from -16.8% and -1.7% in CY23.

Sustainability The Bank has no near-term plans for physical expansion and will continue operating through its existing network of 25 branches. Instead, it is strategically shifting focus toward digital transformation, prioritizing self-banking facilities and technology-driven solutions to enhance customer convenience and operational efficiency.

Financial Risk

Credit Risk The Bank's gross Stage 3 loans rose to ~33.0% of total advances in CY24, up from ~26.0% in CY23 (3MCY25: ~36.0%). A significant portion (~60%) of these non-performing loans relates to EPF-backed facilities, where borrowers often rely on EPF balances for loan settlement. Excluding EPF exposures, the gross NPL ratio stood at a lower ~17.0% in CY24. However, NPL ratio is still above the industry average.

Market Risk The Bank's investment portfolio is primarily composed of Government Securities ("GS") and Unit Trusts. Exposure to GS rose from LKR~2.6bn in CY22 to LKR~2.0bn in CY23, before moderating to LKR~8.9bn in CY24. GS have consistently accounted for over ~92% of the total investment portfolio.

Liquidity And Funding The Bank remains highly reliant on deposits, which accounted for approximately ~99.7% of its funding as of CY24. Its funding strategy is predominantly deposit-driven, with a strong emphasis on retail and savings deposits. Liquidity Coverage Ratio ("LCR") as of CY24 clocked in at ~104.8% (3MCY25: ~127.6%) above the minimum requirement of 100% of CBSL.

Capitalization As of CY24, SMIB's CAR stood at approximately ~18.9%, up from ~17.3% in CY23 (3MCY25: ~17.9%), exceeding the CBSL's minimum requirement of 12.5%. Similarly, the Bank's Tier 1 Capital improved to ~18.9% in CY24 from ~17.2% in CY23 (3MCY25: ~19.6%), against a regulatory minimum of 8.5%. Despite meeting ratio-based thresholds, SMIB faces a capital shortfall relative to the CBSL-mandated minimum capital requirement of LKR~7.5bn. To address this, the Bank has requested a five-year extension from CBSL to meet the requirement through internal capital generation.

LRA

Financials (Summary) in LKR mln

Lanka Rating Agency

State Mortgage and Investment Bank	Dec-24	Dec-23	Dec-22	Dec-21
#	12M	12M	12M	12M
A BALANCE SHEET				
1 Stage I | Advances - net	24,125	24,580	28,035	27,784
2 Stage II | Advances - net	4,945	4,894	3,284	2,410
3 Stage III | Advances (NPLs)	14,738	10,659	9,055	8,895
4 Stage III | Impairment Provision	(2,078)	(1,530)	(1,106)	(987)
5 Investments	11,236	14,784	2,275	2,023
6 Debt Instruments	691	936	300	-
7 Other Earning Assets	153	2,923	13,002	11,775
8 Non-Earning Assets	1,859	1,819	2,115	1,423
Total Assets	55,669	59,067	56,960	53,323
6 Deposits	48,160	52,138	49,140	45,738
7 Borrowings	141	182	301	302
8 Other Liabilities (Non-Interest Bearing)	1,947	1,292	1,049	999
Total Liabilities	50,248	53,612	50,490	47,039
Equity	5,421	5,454	6,474	6,284
B INCOME STATEMENT				
1 Mark Up Earned	7,591	9,324	7,402	5,254
2 Mark Up Expensed	(5,392)	(8,733)	(5,463)	(2,951)
3 Non Mark Up Income	582	276	115	172
Total Income	2,781	867	2,054	2,474
4 Non-Mark Up Expenses	(1,803)	(1,471)	(1,540)	(1,490)
5 Provisions/Write offs/Reversals	(541)	(561)	(366)	(362)
Pre-Tax Profit	437	(1,165)	148	621
6 Taxes on Financial Services	(278)	0	(237)	-
Profit Before Income Taxes	158	(1,165)	(89)	621
7 Taxes	(126)	162	291	(368)
Profit After Tax	33	(1,003)	202	253
C RATIO ANALYSIS				
1 Revenues				
Advances' Yield	11.1%	13.9%	11.9%	11.9%
Spread | Asset Yield - Cost of Funds	6.3%	2.5%	4.8%	5.7%
2 Performance				
Cost of Funds [Mark Up Expensed / Average (Deposits + Borrowings)]	10.7%	17.2%	11.4%	6.4%
ROE	0.6%	-16.8%	3.2%	4.1%
3 Capital Adequacy				
Capital Adequacy Ratio	19.2%	17.3%	21.0%	23.6%
Net Stable Funding Ratio [Available Stable Funding / Required Stable Funding]	108.0%	129.0%	104.0%	136.0%
4 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	17.7%	27.3%	31.2%	30.2%
Demand & Saving Deposit Coverage Ratio	2.4	6.5	7.6	5.3
Top 20 Deposits / Deposits	35.8%	38.9%	34.5%	37.1%
5 Credit Risk				
Impaired Loan Ratio | [Stage III | Advances (NPLs) / Gross Advances]	33.0%	26.0%	22.0%	22.5%
Provision Coverage Ratio | [Impairment Provision / Stage III | Advances (NPLs)]	14.1%	14.4%	12.2%	11.1%

LKR mln

Credit Rating

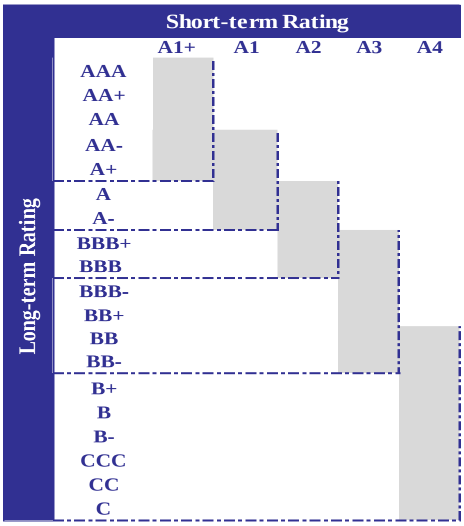
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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