



**RAM RATINGS ASSIGNS P1 RATING TO MERCANTILE INVESTMENTS'
PROPOSED DEBT FACILITY; EXISTING RATINGS REAFFIRMED WITH
NEGATIVE OUTLOOK**

RAM Ratings has assigned a short-term rating of P1 to Mercantile Investments Limited's ("MIL" or "the Company") proposed maiden issuance of LKR 250 million of commercial papers. The assigned rating is at par with MIL's short-term financial institution rating, as the proposed paper ranks *pari passu* with the Company's other senior unsecured debts. Meanwhile, RAM Ratings has reaffirmed MIL's respective long- and short-term financial institution ratings at A (with a negative outlook) and P1. The negative outlook on the long-term rating reflects the Company's waning profit performance over the past few years. Nonetheless, the ratings are still supported by MIL's sturdy capitalisation and adequate liquidity position.

The recent slowdown in loan expansion has taken a toll on MIL's margins. The Company's pre-tax profit declined to LKR 231.39 million in FYE 31 March 2008 ("FY Mar 2008"), compared to LKR 360.78 million in FY Mar 2006. Consequently, MIL's return on assets also eased from 6.53% to 2.95% over the same period. The Company's profit performance was mostly affected by increased funding costs and additional provisioning required by a higher incidence of defaults.

Meanwhile, MIL's asset quality, which had previously been improving, altered its course in FY Mar 2008. The Company's gross non-performing-loan ("NPL") ratio - which had been trending downwards earlier - rose to 7.64% as at end-FY Mar 2008 (end-FY Mar 2007: 6.05%), i.e. above the industry average as at the same date. Nonetheless, RAM Ratings opines that MIL's sturdy capitalisation acts as a cushion in protecting its asset quality.

Thus notably, MIL's key rating driver is still its robust capitalisation, underpinned by the management's prudent retention policies. As at end-FY Mar 2008, the Company's core capital base (shareholders' funds excluding revaluation reserves) stood at an impressive LKR 1.55 billion, translating into a strong Tier-1 risk-weighted capital-adequacy ratio of 20.06%. At the same time, its liquid assets remained at an adequate level and above the statutory minimum of 15% throughout the fiscal year.

Established in 1964 as a financier of motor vehicles, MIL has evolved into one of the top 5 registered finance companies in Sri Lanka. The Company accounts for almost 6% of the industry's assets, in a sector where the 2 largest players combined take the lion's share of over 50%. Through the years, MIL has also built up a solid franchise vis-à-vis the import, sale and financing of motor vehicles in the country.