



## **LRA reaffirms BBB<sub>3</sub>/L3 ratings to Asian Finance Limited**

LRA has reaffirmed the BBB<sub>3</sub> long-term financial institution rating (with a negative outlook) and L3 short-term rating of Asian Finance Limited (“Asian Finance” or “the Company”). The negative outlook is premised on the changing risk profile of the Company, as reflected by its substantial investments in shares and subsequent provisions for losses, coupled with increased real-estate investments and the resultant concentration risk. These had weakened the capitalisation position of Asian Finance during the year under review.

The Company’s gross investment in quoted shares increased from Rs 8.99 million to Rs 61.04 million in FYE 31 March 2006 (“FY Mar 2006”). LRA considers this as a substantial level of investment as it constituted about 34% of Asian Finance’s shareholders’ funds (Rs 148.10 million) as at end-FY Mar 2006; hence, this is a concern. Moreover, the Company had also provided Rs 19.07 million for diminution in the value of these investments; this quantum constituted 32.26% of its pre-tax profits. Our concerns are aggravated by the fact that these investment decisions had been made by a single individual, who also manages this portfolio.

Furthermore, the Company had focused on real-estate development during the year, which had increased to 34.05% (Rs 764.99 million) of its asset base from 20.32% (Rs 344.19 million) the year before. This increase was mainly due to the purchase of a 4-storey office building for Rs 183.83 million - the single largest investment in the Company’s history. Subsequent to the purchase, however, the location has become a “high-security zone” and has dimmed its immediate sale prospects. The property, financed by a term-loan, already accounts for 24.03% of the Company’s total real-estate investments; with the ongoing capitalisation of its cost, this could lead to concentration risk.

On the other hand, the Company’s gross non-performing-loan (“NPL”) ratio eased from 11.74% to 10.78%, although its gross NPL coverage remained low at 47.57%. Return on assets (“ROA”) had also improved to 3.0% (FY Mar 2005: 2.48%) and was driven by real-estate income which, however, introduces earnings volatility. Nevertheless, asset expansion remained restricted by Asian Finance’s weak capital position.

Elsewhere, the management has proposed to merge Asian Finance with its parent company, Ceylinco Securities and Financial Services Limited (“CSFS Limited”). The boards of both entities have agreed to the merger in principal, and are now awaiting approval from the relevant authorities. After the requisite nods, all the assets and liabilities of Asian Finance will be transferred to CSFS Limited, and the Company will cease to exist. Under such circumstances, LRA will no longer have any rating obligations on Asian Finance.

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LRA is a domestic credit rating agency licensed by the Securities and Exchange Commission of Sri Lanka. LRA is a 100%-owned subsidiary of Rating Agency Malaysia Berhad ("RAM"), Malaysia's premier rating agency. RAM is also an affiliate of Standard & Poor's, the world's largest rating agency.

LRA is backed by a 40-strong team of analysts at RAM, which has rated almost all the financial institutions in Malaysia and more than 1,000 debt issues by corporates, statutory organisations and subsidiaries of foreign multinationals. These issuers are involved in the leading sectors of the Malaysian economy, which share some similarities with the potential growth sectors in Sri Lanka. In particular, LRA can leverage on RAM's fortes in the ratings of financial institutions, asset-backed securities and Islamic debt securities.

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