



## RATING ACTION COMMENTARY

# Fitch Upgrades Ideal Finance to 'BB-(Ika)'; Rating Watch Positive

Wed 10 Jun, 2020 - 10:29 AM ET

Fitch Ratings - Colombo - 10 Jun 2020: Fitch Ratings Lanka has upgraded Ideal Finance Limited's National Long-Term Rating to 'BB-(Ika)', from 'B+(Ika)'. The rating is on Rating Watch Positive (RWP).

The upgrade is supported by an improved credit profile, but follows the recalibration of Sri Lanka's national ratings scale to reflect changes in the relative creditworthiness of Sri Lankan issuers after Fitch downgraded the country's sovereign rating to 'B-/Negative', from 'B/Negative', on 24 April 2020.

## KEY RATING DRIVERS

The upgrade reflects improved capitalisation following the introduction of new capital after an initial LKR1.1 billion investment in February 2020 from India's Mahindra & Mahindra Financial Services Limited (MMFSL). This strengthens the company's standalone profile and bolsters loss-absorption buffers against Sri Lanka's challenging operating environment. The Central Bank of Sri Lanka has also removed the LKR700 million cap on total deposits due to Ideal's compliance with the interim minimum capital requirement.

The RWP reflects Fitch's belief that Ideal's rating could benefit from the change in shareholding and increased probability of support once MMFSL's effective

control is established in light of MMFSL's potentially stronger credit profile. MMFSL will progressively invest LKR2 billion (approximately USD11 million) to acquire a 58.2% stake in Ideal in three tranches up to 2021. Fitch expects the minimum regulatory capital requirement of LKR2.5 billion for finance companies to be met at the end of the transaction, at which point we expect MMFSL to have acquired effective control of Ideal.

## **RATING SENSITIVITIES**

Factors that could, individually or collectively, lead to positive rating action/upgrade:

We expect to resolve the RWP once we conclude our assessment of MMFSL's ability to provide support to Ideal and have greater clarity on the linkages between Ideal and MMFSL. Fitch will maintain the RWP beyond the typical six-month horizon, with parental support likely to be factored into the rating once MMFSL has acquired effective control of Ideal. Fitch's view of support will include an assessment the level of strategic importance of the Sri Lankan market and Ideal to MMFSL, the extent of integration, branding and provision of broader funding support.

Fitch will remove the RWP if the investment is not completed. The rating would then remain driven by Ideal's intrinsic credit profile.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

Ideal's rating is currently driven by its standalone profile. Negative rating action could occur if a severe deterioration in the operating environment, beyond our base-case expectations, were to diminish the company's asset quality, profitability and capital adequacy, leading to downward pressure on Ideal's standalone profile.

## **BEST/WORST CASE RATING SCENARIO**

International scale credit ratings of Financial Institutions issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th

percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

## REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

## RATING ACTIONS

ENTITY/DEBT	RATING
Ideal Finance Limited	Natl BB-(lka) Rating Watch Positive Upgrade LT

[VIEW ADDITIONAL RATING DETAILS](#)

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## APPLICABLE CRITERIA

[Non-Bank Financial Institutions Rating Criteria \(pub. 29 Feb 2020\) \(including rating assumption sensitivity\)](#)

[Bank Rating Criteria \(pub. 29 Feb 2020\) \(including rating assumption sensitivity\)](#)

[National Scale Rating Criteria \(pub. 08 Jun 2020\)](#)

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Ideal Finance Limited

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Non-Bank Financial Institutions

Asia-Pacific

Sri Lanka

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