

## RATING ACTION COMMENTARY

# Fitch Affirms Siyapatha Finance at 'BBB+(Ika)'; Outlook Stable

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Fitch Ratings - Colombo - 25 Apr 2024: Fitch Ratings has affirmed Siyapatha Finance PLC's National Long-Term Rating at 'BBB+(Ika)' with a Stable Outlook. Fitch also affirmed Siyapatha's subordinated debt at 'BBB-(Ika)' and proposed senior debt at 'BBB+(EXP)(Ika)'.

## KEY RATING DRIVERS

**Shareholder Support Drives Ratings:** Siyapatha's rating is driven by our expectation that its parent, Sampath Bank PLC (A(Ika)/Stable), would provide extraordinary support to Siyapatha, if required. Sampath's ability to support its subsidiary is reflected in its rating and Siyapatha's relatively modest size. Our support assessment also considers Sampath's full ownership of Siyapatha, record of equity support and combined branding.

**Limited Subsidiary Role:** Siyapatha is rated two notches below Sampath due to its limited importance to the group. Siyapatha mainly caters to retail and SME customers that are beyond the Sampath's risk appetite and its core leasing business accounted for a modest 5.6% of group loans at end-2023. The company made up 2.9% of Sampath's consolidated assets and contributed 4.2% to the group's pre-tax profit. Siyapatha has significant management independence and limited operational integration with its parent bank.

**Weak Standalone Profile:** We assess Siyapatha's standalone credit profile to be weaker than its support-driven rating, due to its moderate franchise, at 2.8% of sector assets, high risk appetite and weak financial profile. This is reflected by an above-industry gross non-performing loan ratio, moderate capital buffers and high leverage. Siyapatha's pre-tax return on average assets marginally improved to 3.7% in 2023, from 3.4% in 2022, amid a gradual net interest margin recovery and lower impairment charges, but remains below the industry average.

**Recovering Non-Performing Loan Ratio:** We expect Siyapatha's gross stage 3 loan ratio to further improve amid a pick-up in business activity and declining interest rates, which should support borrower repayment capacity and loan collections. The ratio stood at 19.3% at end-2023, down from 25.8% a year ago, but was still above the 17.8% sector average. The decline in non-performing loans was driven by Siyapatha's sustained recovery efforts and improved economic indicators in the past few quarters relative to the stress in 2022 and 1H23.

**Moderate Capital Buffers:** Siyapatha's regulatory capital ratios benefit from the lower risk weight of gold-backed lending, which accounts for around 20% of gross loans, but aggressive growth in non-gold products may exert some pressure. Siyapatha's debt/tangible equity of 5.1x at end-2023 (end-2022: 5.5x) remained higher than the Fitch-rated peer average. The core capital ratio improved moderately to 17.1%, from 16.1% at end-2022, but was below the industry average of 21.2%.

**Improved Financial Flexibility:** We expect Siyapatha to maintain its funding mix and continue to benefit from the perceived shareholder support from Sampath. Increased deposit mobilisation efforts saw deposits reach 64% of total funding in 2023, up from 55% in 2022. An improved market liquidity also benefits the company's access to wholesale term borrowings, similar to peers. As a result, financial flexibility has improved, with reduced reliance on secured wholesale borrowings.

## **RATING SENSITIVITIES**

### **Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade**

Siyapatha's rating is sensitive to changes in Sampath's credit profile, as reflected in the parent's National Long-Term Rating, as well as Fitch's opinion around Sampath's ability and propensity to extend timely extraordinary support. Developments that could lead to negative rating action include:

- meaningful reduction in the parent's ownership, control or influence that could weaken its propensity to support the subsidiary
- notable decline in Siyapatha's capital buffers, indicating reduced timeliness in financial support to back growth or meet regulatory norms
- sustained weak performance of Siyapatha that we believe will weaken the parent's propensity to support the subsidiary

- a large increase in size relative to the parent that makes extraordinary support more onerous

- insufficient or delayed liquidity support from the parent relative to Siyapatha's needs that hinders Siyapatha's ability to meet its obligations in a timely manner

Such developments could significantly reduce shareholder support prospects and, if severe, lead to a multi-notch downgrade.

### **Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade**

An upgrade would most likely result from an upgrade of Sampath's National Long-Term Rating, which would indicate the parent's strengthened ability to support the subsidiary.

An upgrade could also stem from a greater propensity to support Siyapatha, due to a significant increase in its strategic importance to Sampath and integration within the group, although we regard this as unlikely in the near term.

### **DEBT AND OTHER INSTRUMENT RATINGS: KEY RATING DRIVERS**

Siyapatha's proposed senior unsecured debenture is rated at the same level as its National Long-Term Rating, as it constitutes its direct, unconditional, unsecured and unsubordinated obligation.

The company's outstanding subordinated debentures are rated two notches below its National Long-Term Rating. We have applied our Bank Rating Criteria in rating these instruments, as we view the prudential capital framework for finance companies to be closer to that for banks in Sri Lanka. This reflects our baseline notching for loss severity for this type of debt and our expectation of poor recoveries in the event of default. There is no additional notching for non-performance risk, as the debentures have no going-concern loss-absorption features, in line with Fitch criteria.

### **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.

### **PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS**

Siyapatha's ratings are driven by Sampath's National Long-Term Rating.

**RATING ACTIONS**

<b>ENTITY / DEBT</b> ⚡	<b>RATING</b> ⚡			<b>PRIOR</b> ⚡
Siyapatha Finance PLC	Natl LT	BBB+(lka) Rating Outlook Stable		BBB+ (lka) Rating Outlook Stable
	Affirmed			
subordinated	Natl LT	BBB-(lka)	Affirmed	BBB-(lka)
senior unsecured	Natl LT	BBB+(EXP)(lka)	Affirmed	BBB+(EXP) (lka)

[VIEW ADDITIONAL RATING DETAILS](#)

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## **APPLICABLE CRITERIA**

[National Scale Rating Criteria \(pub. 22 Dec 2020\)](#)

[Non-Bank Financial Institutions Rating Criteria \(pub. 18 Jan 2024\) \(including rating assumption sensitivity\)](#)

[Bank Rating Criteria \(pub. 16 Mar 2024\) \(including rating assumption sensitivity\)](#)

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