

05 Aug 2019 | Affirmation

Fitch Affirms Ideal Finance's 'B+(lka)' Rating; Outlook Stable

Fitch Ratings-Colombo-06 August 2019: Fitch Ratings Lanka has affirmed Ideal Finance Limited's National Long-Term Rating at 'B+(lka)' with a Stable Outlook.

KEY RATING DRIVERS

Ideal's National Long-Term rating reflects its high-risk appetite, with significant exposure to the more-vulnerable segments of the finance and leasing market and aggressive growth. The rating also captures the company's still-developing franchise, which is reflected in its small market share and limited operating history.

Fitch expects Ideal's asset quality to remain under pressure due to its unseasoned loan book following sustained rapid loan expansion amid a weak operating environment. Its reported non-performing loan ratio (greater than 180 days overdue) increased to 2.7% in the financial year ended March 2019 (FY19) (FY18: 1.6%). Fitch sees Ideal's exposure to non-core real-estate investments (6% of equity at FYE19) as a risk due to its cyclical nature.

Fitch expects Ideal to raise capital to meet the regulatory minimum core capital requirement for licensed finance companies as its internal capital generation is unlikely to be sufficient. It fell short of the LKR1.5 billion interim requirement by 1 January 2019, and its non-compliance could give rise to regulatory risks. Ideal's leverage in terms of debt/tangible equity (FYE19: 2.5x; FYE18: 1.9x) could be supported by possible equity infusions but it is likely to increase in the medium-term as the company builds scale.

Ideal's profitability in terms of pre-tax net income/average assets has improved (FYE19: 6.0%; FYE17: 4.2%) supported by higher interest margins. Its profitability could come under pressure from rising credit costs amid asset-quality pressures.

Ideal's financial flexibility remains low compared with that of higher rated peers due to its reliance on secured funding. Deposits accounted for 21% of its total funding at FYE19 and its deposit base remains highly concentrated. Ideal is most likely to depend on non-deposit funding to fund its loan book in the medium term.

Ideal is one of the smallest finance companies in Sri Lanka, accounting for only 0.3% of total sector assets at FYE19.

RATING SENSITIVITIES

An increase in Ideal's operating scale alongside stronger capitalisation and a moderation in risk appetite could lead to a rating upgrade.

Deterioration in Ideal's capital buffers through a significant deterioration in asset quality or an increase in risk appetite through, for instance, an aggressive ramp-up in real-estate investments, could lead to a rating downgrade.

Issuer Disclosure on Regulatory Action

The Central Bank of Sri Lanka has imposed a cap of LKR700 million on total deposits due to Ideal's non-compliance with the interim minimum capital requirement of LKR1.5 billion.

The 'Issuer Disclosure on Regulatory Action' heading was provided by the issuer and is included pursuant to applicable regulatory requirements. Fitch Ratings Lanka is not responsible for the contents of such information.

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Applicable Criteria

[Bank Rating Criteria \(pub. 12 Oct 2018\)](#)

[National Scale Ratings Criteria \(pub. 18 Jul 2018\)](#)

[Non-Bank Financial Institutions Rating Criteria \(pub. 12 Oct 2018\)](#)

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