

Rating Action: Moody's places ratings of three Sri Lankan banks on review for downgrade; downgrades Bank of Ceylon's BCA to b3 from b2

20 Apr 2020

Singapore, April 20, 2020 -- Moody's Investors Service has placed the B2 long-term local currency deposit and foreign currency issuer ratings of Bank of Ceylon (BOC), Hatton National Bank Ltd. (HNB) and Sampath Bank PLC (Sampath) on review for downgrade.

At the same time, Moody's has downgraded the Baseline Credit Assessment (BCA) of BOC to b3 from b2 and placed it on review for further downgrade. Moody's has also placed the b2 BCAs of HNB and Sampath on review for downgrade.

The outlooks have been changed to rating under review from stable.

The rating actions follow Moody's placement of Sri Lanka's B2 sovereign rating on review for downgrade. For more information on the sovereign rating action, please refer to the Government of Sri Lanka issuer page on www.moody.com.

A full list of the ratings is provided at the end of this press release.

RATINGS RATIONALE

The decision to place the banks' assessments and ratings on review for downgrade reflects Moody's placement of Sri Lanka's B2 sovereign rating on review for downgrade. Moody's believes that there is a high level of dependency between the creditworthiness of Sri Lankan banks and that of the sovereign, because the banking operations are largely domestic and the banks hold significant amounts of sovereign debt. In addition, the sovereign's credit strength is a key input to Moody's assessment of the government's ability to support the banks in times of need.

The rapid and widening spread of the coronavirus outbreak, deteriorating global economic outlook, volatile oil prices, and asset price declines are creating a severe and extensive credit shock across many sectors, regions and markets. The Sri Lankan banking system has been one of the sectors affected by the shock, given Sri Lanka's weak economy and heavy reliance on external borrowings. Moody's regards the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. Today's action also incorporates the negative impact on BOC, HNB and Sampath of the breadth and severity of the shock, and the likely deterioration in the banks' asset quality and in the government's ability to support these banks in times of need.

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Sri Lanka's already weak economy will take a further hit from the widespread disruption to tourism, export-oriented sectors and domestic activities because of the coronavirus pandemic. The deterioration in macroeconomic conditions also has the potential to substantially weaken the banks' asset quality and profitability. At the same time, the risk-off sentiment among global investors could also hinder the government's access to external borrowings, exacerbating the deterioration in the government's fiscal position and ability to support the banks in times of need. The degree of negative impact will depend on the length of the disruption, which is uncertain at this point.

The downgrade of BOC's BCA mainly reflects the deterioration in the bank's asset quality, as well as the bank's low capitalization when compared to its Sri Lankan peers. BOC's problem loan ratio, based on the proportion of stage 3 loans under the equivalent of IFRS (International Financial Accounting Standard) 9, rose to more than 10% as of 31 December 2019 from 9.2% a year ago amid subdued tourism activity following the Easter Sunday 2019 terrorist attack. The bank's Common Equity Tier 1 ratio of 11.4% as of 31 December 2019 is also modest relative to the rated peer average of 13.4%, reflecting a weak loss buffer amid a deteriorating operating environment. Despite its weakening solvency, Moody's expects the bank's funding and liquidity will

remain stable over the next 12-18 months.

Moody's incorporates a very high probability of government support in the ratings of BOC, reflecting the bank's systemic importance as the largest bank in Sri Lanka and the government's full ownership of the bank. As a result, BOC's B2 long-term local currency deposit and foreign currency issuer ratings are one notch higher than the bank's BCA.

While Moody's incorporates a high probability of government support in the long-term local currency deposit and foreign currency issuer ratings of HNB and Sampath, in line with the banks' sizable market shares in terms of deposits, the ratings do not benefit from any uplift because the banks' BCAs are already at the same level as the sovereign rating.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Given the review for downgrade, the banks' BCAs and long-term ratings are unlikely to be upgraded during the review period. Nevertheless, Moody's could confirm the ratings with either a stable or negative outlook if the coronavirus situation eases and the impact on Sri Lanka's economy and the government's ability to refinance its debts is not as severe as Moody's currently anticipates.

A downgrade of the sovereign rating could lead to a downgrade of the banks' BCA and long-term ratings. Moody's could also downgrade the banks' BCAs if there is a material deterioration in asset quality. A significant decline in capitalization will also exert downward pressure on the banks' BCAs.

The principal methodology used in these ratings was Banks Methodology published in November 2019 and available at https://www.moodys.com/research/Banks-Methodology--PBC_1147865. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Bank of Ceylon, headquartered in Colombo, reported total assets of LKR2,462 billion at 31 December 2019.

Hatton National Bank Ltd., headquartered in Colombo, reported total assets of LKR1,196 billion at 31 December 2019.

Sampath Bank PLC, headquartered in Colombo, reported total assets of LKR999 billion at 31 December 2019.

Issuer: Bank of Ceylon

... Adjusted Baseline Credit Assessment, Downgraded to b3 from b2; Placed Under Review for further Downgrade

... Baseline Credit Assessment, Downgraded to b3 from b2; Placed Under Review for further Downgrade

... Long-term Counterparty Risk Assessment, Downgraded to B2(cr) from B1(cr); Placed Under Review for further Downgrade

... Short-term Counterparty Risk Assessment, Affirmed NP(cr)

... Long-term Counterparty Risk Rating (Foreign and Local Currency), Downgraded to B2 from B1; Placed Under Review for further Downgrade

... Short-term Counterparty Risk Rating (Foreign and Local Currency), Affirmed NP

... Long-term Issuer Rating (Foreign Currency), Placed on Review for Downgrade, currently B2, Outlook Changed To Rating Under Review From Stable

... Long-term Deposit Rating (Foreign Currency), Placed on Review for Downgrade, currently B3, Outlook Changed To Rating Under Review From Stable

... Long-term Deposit Rating (Local Currency), Placed on Review for Downgrade, currently B2, Outlook Changed To Rating Under Review From Stable

... Short-term Deposit Rating (Foreign and Local Currency), Affirmed NP

... Outlook, Changed To Rating Under Review From Stable

Issuer: Hatton National Bank Ltd.

... Adjusted Baseline Credit Assessment, Placed on Review for Downgrade, currently b2

... Baseline Credit Assessment, Placed on Review for Downgrade, currently b2

... Long-term Counterparty Risk Assessment, Placed on Review for Downgrade, currently B1(cr)

... Short-term Counterparty Risk Assessment, Affirmed NP(cr)

... Long-term Counterparty Risk Rating (Foreign and Currency), Placed on Review for Downgrade, currently B1

... Short-term Counterparty Risk Rating (Foreign and Local Currency), Affirmed NP

... Long-term Issuer Rating (Foreign Currency), Placed on Review for Downgrade, currently B2, Outlook Changed To Rating Under Review From Stable

... Long-term Deposit Rating (Foreign Currency), Placed on Review for Downgrade, currently B3, Outlook Changed To Rating Under Review From Stable

... Long-term Deposit Rating (Local Currency), Placed on Review for Downgrade, currently B2, Outlook Changed To Rating Under Review From Stable

... Short-term Deposit Rating (Foreign and Local Currency), Affirmed NP

... Outlook, Changed To Rating Under Review From Stable

..Issuer: Sampath Bank PLC

... Adjusted Baseline Credit Assessment, Placed on Review for Downgrade, currently b2

... Baseline Credit Assessment, Placed on Review for Downgrade, currently b2

... Long-term Counterparty Risk Assessment, Placed on Review for Downgrade, currently B1(cr)

... Short-term Counterparty Risk Assessment, Affirmed NP(cr)

... Long-term Counterparty Risk Rating (Foreign and Local Currency), Placed on Review for Downgrade, currently B1

... Short-term Counterparty Risk Rating (Foreign and Local Currency), Affirmed NP

... Long-term Issuer Rating (Foreign Currency), Placed on Review for Downgrade, currently B2, Outlook Changed To Rating Under Review From Stable

... Long-term Deposit Rating (Foreign Currency), Placed on Review for Downgrade, currently B3, Outlook Changed To Rating Under Review From Stable

... Long-term Deposit Rating (Local Currency), Placed on Review for Downgrade, currently B2, Outlook Changed To Rating Under Review From Stable

... Short-term Deposit Rating (Foreign and Local Currency), Affirmed NP

... Outlook, Changed To Rating Under Review From Stable

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1133569.

At least one ESG consideration was material to the credit rating action(s) announced and described above.

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