



## **Fitch Affirms Sri Lanka's People's Bank at 'AA+(lka)'; Outlook Negative**

Fitch Ratings - Colombo - 27 Jul 2020: Fitch Ratings has affirmed the National Long-Term Rating of People's Bank (Sri Lanka) (PB) at 'AA+(lka)'. The Outlook is Negative.

### **KEY RATING DRIVERS**

PB's National Long-Term Rating is driven by Fitch's expectations of extraordinary support from the sovereign. The state's high propensity for support stems from PB's high systemic importance as the second-largest bank in the country, accounting for nearly 16% of domestic banking system assets at end-March 2020. It also takes into account its quasi-sovereign status, its role as a key lender to the government and full government ownership. The state's limited ability to provide extraordinary support is reflected in its rating.

The Negative Outlook reflects the risk that PB could be downgraded should there be negative rating action on the Sri Lankan sovereign (B-/Negative) that results in a reassessment of the rating relativities among the universe of Sri Lankan issuers.

Fitch regards PB's intrinsic financial strength as weaker than the support-driven rating of 'AA+(lka)' due to the weaker financial profile relative to the larger private banks in terms of its capitalisation and asset quality. This is despite PB's stronger franchise, which supports its profitability and funding profile. We assess PB's capitalisation as weaker than the reported common equity Tier 1 ratio of 11.2% at end-1Q20. The bank's reported capital ratios are supported by the low risk-weighted asset density relative to the peers because of the substantial exposure - risk-weighted at mostly 0% - to the state and state-owned entities. As such, we believe that PB's capital buffers are thin on an adjusted basis. We expect PB to rely mainly on internally generated capital to sustain core capital levels in the medium term given the heightened constraint on accessing capital from the state.

Fitch expects PB's significant exposure to the state and state-owned enterprises to further increase in the near to medium term, because of the sovereign's deteriorating fiscal position and the bank's strong linkages to the government. State exposure was already high at 38% of gross loans at end-2019, indicating high concentration risk and the bank's dependency on the state's financial profile.

We expect the coronavirus pandemic's impact on the economy to intensify pressure on the bank's asset quality. PB's stage 3 loans (impaired loans)/gross loans ratio, increased to 10% by end-2019 (2018: 9.5%), which is already higher compared with larger private banks' average of 8%, and we expect this to rise further due to increased delinquencies from retail and SME segments, where the bank has significant exposure.

## RATING SENSITIVITIES

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

Upside to PB's National Long-Term Rating is limited in the near term, due to our assessment of the sovereign rating and the operating environment outlook, both of which are negative. A revision of the sovereign rating Outlook to Stable is the most likely driver for stabilising the Outlook on PB.

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

Pressure on PB's National Long-Term Rating could stem from a downgrade of Sri Lanka's sovereign rating. A sovereign rating downgrade to 'CCC+' or below would make it unlikely that we would factor in expectations of support to any bank in Sri Lanka and it will also likely constrain the standalone credit profiles of domestic banks.

PB has a 1.78% equity stake in Fitch Ratings Lanka Ltd. No shareholder other than Fitch, Inc. is involved in the day-to-day rating operations of, or credit reviews undertaken by, Fitch Ratings Lanka Ltd.


## 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

PB's National Rating is driven by the sovereign rating.

### RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
People's Bank (Sri Lanka)	Natl LT	AA+(Ika) 	Affirmed	AA+ (Ika) 

## VIEW ADDITIONAL RATING DETAILS

Additional information is available on [www.fitchratings.com](http://www.fitchratings.com)

## APPLICABLE CRITERIA

- [Bank Rating Criteria \(pub. 28 Feb 2020\) \(including rating assumption sensitivity\)](#)
- [National Scale Rating Criteria \(pub. 08 Jun 2020\)](#)

## ADDITIONAL DISCLOSURES

- [Solicitation Status](#)
- [Endorsement Policy](#)

## ENDORSEMENT STATUS

People's Bank (Sri Lanka) -

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