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CTOS Digital Bhd's ambitions of growing into the realm of corporate credit ratings is accelerating.

This week, the consumer credit specialist said it will be making a general offer for the rest of the shares it does not own in RAM Holdings Bhd, which owns RAM Rating Services Bhd, and which in turn is the leading

CTOS targets SMEs through RAM acquisition

Preserving independence of the debt rating agency key

homegrown debt rating agency in the country.

CTOS currently owns a 19.23% stake in RAM. On Thursday, CTOS said based on preliminary feedback, it may achieve more than 51% shareholding in RAM.

The rationale for the move is clear. In a statements issued by CTOS, it says that as one of Asean's leading financial and data solutions groups, it is well-positioned to work closely with RAM to develop new rating solutions for companies, small and medium-sized enterprises (SMEs) in particular, so that they can access broader forms of credit and grow their businesses.

"This in turn will accelerate RAM's growth and establish it as the leading rating agency, not just in Malaysia but regionally," CTOS said in a June 9 statement.

Although Malaysia is a leading corporate debt market, with sukuk offerings often winning records and accolades, issuers have largely remained the large corporations. This means that the debt market via bonds remains largely untapped for smaller companies or SMEs, which make up the bulk of businesses in Malaysia and South-East Asia.

Locally, banking institutions are the main source of financing for SMEs, providing more than 90% of total financing.

The reasons for this are a few. SMEs generally require smaller amounts of funds and most of the products in the market seem to be tailored for larger companies.

The other factor is credit issues.

"Bond investors want to make secure investments and hence prefer to buy the papers issued by companies with good credit ratings", says an industry observer.

The World Bank in a September 2020 report on Malaysia's domestic bond market notes the deal-size bias. It says that outsized portfolios of big institutional investors like the Employees Provident Fund (relative to the size of the domestic market) and the investment limits imposed by their investment mandates have ensured tepid interest in small debt issues.

"This disinterest has prompted arrangers to focus on larger issues, giving preference to those exceeding RM250mil, a striking change from the pre-Asian financial crisis average of RM100mil," the international financial

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Suresh Menon

institution states.

This situation, according to the World Bank, discourages corporates with smaller working capital or capital requirements from tapping into the local bond market. The additional liquidity premium demanded by investors may also make the issuing of debt papers cost more.

"Against such a backdrop, bigger conglomerates may be the only ones that can access bond financing. But with governments now struggling to cope with economies overwhelmed by coronavirus, financing the needs of SMEs through the bond market is an even more urgent need now," it points out.

All this illustrates the opportunities that CTOS and RAM are likely to tap.

CTOS, which is 30.26% owned by private equity firm Creador via Inodes Ltd, first emerged in RAM in July last year when it acquired 4.6% from CIMB Bank Bhd for RM10.1mil. It was the group's first acquisition after its listing in the previous month at an offer price of RM1.10.

From here, the group has been raising its stake in the rating agency and made other acquisitions as well.

Based on an April analyst report, CTOS' acquisition of a 17.23% stake in RAM (from 8.1% at that point) cost it RM25mil or about 33 times price to earnings. This according to the research firm was fair and in line with other listed global credit rating agencies.

Now CTOS is making a move to acquire a majority stake in RAM beyond the 20% cap on individual shareholding.

CTOS commenced the investment application on April 15, 2021 and said it undertook a "rigorous process" with the Securities Commission (SC) to determine how it could

add value to RAM. The SC has given CTOS the nod to own a majority stake in RAM, while shareholders of RAM approved the amendments to its constitution to remove the 20% cap on shareholding in the company at an AGM last week.

RAM has 13 shareholders with four owning more than a 10% stake. Through its unit Oscar Matrix Sdn Bhd, Creador, which was founded by Brahmam Vasudevan, holds 19.9% in RAM.

Besides CTOS and Oscar Matrix, the other substantial shareholders of RAM include S&P Global Asian Holdings Pte Ltd (19.2%), Dragonline Solutions Sdn Bhd (15.65%) and Hong Leong Bank Bhd with 5.8% stake.

A capital market observer says that the 20% cap was a "tangible wall" to preserve the independence and sanctity of a rating. By removing this and allowing a listed entity to have a controlling stake, will it mean more aggressive marketing going forward to maximise returns, which could result in unfair competition for the smaller Malaysian Rating Corporation Bhd (MARC), he asks.

Independence is the critical aspect

Suresh Menon, the former executive director of RAM and one of the agency's founding staff when it was set up in 1990, thinks it does not matter what sort of constitutional limit there is.

"As far as I am concerned, it (the 20% limit on individual shareholding) should not be there. The more critical aspect is whether the entity can maintain the independence of the agency," he told *StarBizWeek* when contacted.

He says checks and balances for RAM are very important and its rating committee must be totally independent.

Suresh recalls that the 20% cap was not there initially. This came about more than two decades later following the entry of S&P.

"When RAM was established by the Malaysian central bank, the understanding was that each shareholder would have a minority stake. The idea was to keep the shareholding spread as much as possible so that no shareholder could exert influence on the company. But constitutionally, the 20% was never there at the beginning," he notes.

The agency, formerly known as Rating Agency Malaysia Bhd, then had 51 shareholders.

Being a credit reference agency, Suresh believes that "CTOS makes a good shareholder to own RAM".

"There are synergies that can be derived. However, if we lift the corporate veil, the ultimate shareholder is Creador, which will be closely watched on how it runs CTOS and in turn RAM," he says.

He explains that rating agencies are also profit-oriented and many are publicly-traded entities elsewhere. The most important thing at the end of the day is about preserving its independence and integrity via checks and balances, he adds.

It should be noted that in its press statements, CTOS has said that it remains committed to maintaining the independence and integrity of RAM, will not get involved in any rating-related decisions nor in any aspect of operations. CTOS also said that it will be only nominating one board member for RAM and not seek to make any changes to the board, leaving the board to make all important financial decisions.

Moving forward, whether more changes in the local debt rating market will follow remains to be seen.

Notably, in 2020, global integrated risk assessment firm Moody's Corp emerged as a shareholder in MARC and now owns a 19.45% stake in the country's second debt rating agency.

The other credit rating agency which has a stake in MARC is Care Ratings Ltd at 10%, while its 22 other shareholders (comprising insurance companies, stockbrokers and investment banks) own less than 5% each.