



Fitch Rates Ferratum Oyj 'BB-'; Outlook Stable

Fitch Ratings-Frankfurt-13 March 2019: Fitch Ratings has assigned Finland-based consumer lender Ferratum Oyj (Ferratum) a Long-Term Issuer Default Rating (IDR) of 'BB-' with Stable Outlook.

Founded in 2005, Ferratum is an online-focused consumer finance company with an international footprint in over 20 countries, including a strong presence in its domestic market Finland, as well as Sweden and Poland. The company is listed on the prime standard segment of the Frankfurt Stock Exchange (with a free float of around 45%) and also incorporates a Malta-domiciled bank (Ferratum Bank p.l.c.) under its wider franchise. Ferratum is majority-owned by its founding CEO (55%).

KEY RATING DRIVERS

IDR

The Long-Term IDR of Ferratum reflects its monoline business model and evolving franchise as a predominantly pan-European online-focussed, specialised consumer lender in a niche market segment, which continues to experience regulatory challenges. The rating reflects Ferratum's adequate through-the-cycle profitability and adequate capitalisation but also takes into account the company's increased appetite for credit risk in its core activities (with an elevated level of past due receivables) and reliance on short-term online retail deposits.

The rating also takes into consideration the company's adequate risk provisioning approach and proactive management stance with regard to non-performing loans. Fitch views the consolidation of Ferratum Bank in the wider company as moderately credit-positive, balancing efficient market and funding access via retail deposits against an increasing need for regulatory compliance (both with regard to capital and liquidity management).

Ferratum primarily serves retail customers likely to fall outside the conventional acceptance parameters of mainstream lenders, with a significant interest premium charged to reflect their non-standard risk profile. The company has expanded significantly in the past four years, leveraging its banking license and elevated capital base after its initial public offering in 2015. Fitch recognises the moderate scale Ferratum has achieved to date; however, we assess the franchise in the context of Ferratum's underlying business model, which is typically subject to limited barriers of entry and an evolving regulatory environment, and therefore prone to some volatility.

The higher-cost credit market has in recent years been subject to regulatory intervention in the form of caps on allowable interest and fee rates in numerous European countries, including some of Ferratum's core markets such as Finland, Sweden, and Latvia. Ferratum has to date been able to reposition itself in the face of such developments, helped by the fairly lean cost structure of its online business model and its broad geographic coverage has historically limited its vulnerability to regulatory shocks in any one geographic market. However, in Fitch's view, regulatory intervention remains an inherent risk in this sector, against which smaller lenders in particular have limited lobbying power.

Ferratum operates in a market segment characterised by a heightened risk appetite within underwriting standards. Consequently, asset quality is inherently weaker than that at commercial banks, with a

comparatively higher proportion of the loan book exhibiting at least partial overdue status (around 50% of the receivable book at end-3Q18 was 30 or more days past due; four-year historical average before IFRS9 adoption at 42.6%). Following the recent adoption of IFRS 9 and associated adjustment to its provisioning approach, Fitch expects the company's asset quality indicators to improve over the short- to medium-term, albeit at the cost of some moderate margin easing. The management of asset quality is also aided by the disposal of non-performing portfolios early in the loan life cycle (i.e. after 90 days past due). Known as contractual forward flow agreements, these are expected to gain in prominence as the company utilises these agreements to comply with tightening ECB-imposed non-performing loan requirements at bank subsidiary level.

Ferratum's profitability margins are adequate by wider finance and leasing company benchmarks, with the company having demonstrated an appropriate profitability track record in an evolving operating environment. Fitch assesses profitability expectations against the company's ability to operate under more conservative provisioning requirements as part of IFRS 9 adoption and the company's intentions to increasingly act as a finance intermediary over the medium- to long-term (focusing on loan origination while limiting own balance sheet exposure).

Ferratum has a largely unsecured funding profile, consisting of retail deposits from its banking subsidiary (EUR174 million as of end-3Q18), senior unsecured bonds (EUR165 million), and a credit line from Nordea (EUR35 million). While the senior bonds have long-term maturities (three to four years), online deposits are mostly shorter-term with 84% expiring within the next three months (as of end-3Q18), which in our view are less sticky than traditional retail deposits (particularly in periods of market stress).

Ferratum's subsidiary bank is also subject to regulatory constraints on moving its deposit funding within the group, including a requirement of equity and non-deposit funding accounting for at least 35% of retail deposits. Ferratum maintains a sizeable cash balance (EUR159 million as of end-3Q18) held predominantly with the Central Bank of Malta to support its liquidity.

Fitch calculates Ferratum's gross debt/tangible equity ratio as of end-3Q18 at around 5x, which corresponds to the upper end of the 'bb' range rating category under the benchmarking ratio for finance and leasing companies. This was moderately higher than the company's historical leverage ratio of around 4x, with the increase in 2018 driven by a bond issue of EUR100 million by Ferratum Capital to lengthen the company's funding profile. Fitch assesses the capitalisation and leverage of Ferratum in the context of its risk appetite, which renders it more susceptible to cyclical performance swings.

RATING SENSITIVITIES

IDR

A worsening of credit losses, notably if combined with looser provisioning standards, pressuring profitability and ultimately eroding Ferratum's capital base, would be negative for the Long-Term IDR.

A protracted weakening of Ferratum's franchise, arising from a sustained loss in revenue, significant operational losses and/or adverse reputational ramifications in connection with the company lending activities could be rating-negative. In addition, a further significant tightening of regulatory requirements in key markets - translating into a significant loss of business and/or notable margin pressure - could result in a rating downgrade.

A marked loss of retail deposits at Ferratum Bank as a key mechanism of funding access for the wider company could be rating-negative. Furthermore, any sustained adverse operational developments at Ferratum Bank level (either of a regulatory nature or with regard to customer confidence), thereby impacting on the company's ability to effectively leverage its banking subsidiary as a market-facing financial services provider could be rating-negative.

A sustained enhancement of Ferratum's franchise by meaningfully growing the company's balance sheet without a marked increase in risk appetite, coupled with a further refinement of underwriting standards and the successful integration of recently established management functions within the wider company, could be rating-positive.

Materially lower consolidated leverage on a sustained basis, in particular if in combination with an enhanced and more resilient franchise, could also support a positive rating action.

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Applicable Criteria
Non-Bank Financial Institutions Rating Criteria (pub. 12 Oct 2018)

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