



Fitch Affirms Ferratum at 'BB-'; Outlook Stable

Fitch Ratings - Frankfurt am Main - 10 March 2020:

Fitch Ratings has affirmed Ferratum Oyj's Long-Term Issuer Default Rating (IDR) and Ferratum Capital Germany GmbH's senior unsecured bond rating at 'BB-'. The Outlook on the Long-Term IDR is Stable.

Ferratum is an online-focused consumer finance company operating in the high-cost credit sector 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 and also incorporates a Malta-domiciled bank (Ferratum Bank p.l.c.) under its wider franchise.

Key Rating Drivers

IDR

Ferratum's Long-Term IDR reflects its monoline business model and evolving franchise as a predominantly pan-European online-focused, specialised consumer lender in a niche market segment, which remains exposed to an evolving regulatory landscape in most of its key target markets. The rating also recognises Ferratum's adequate through-the-cycle profitability and adequate capitalisation but equally takes into account the company's heightened appetite for credit risk in its core activities (operating as a finance provider in a high-cost credit segment) and reliance on short-term online retail deposits for funding purposes.

Fitch currently rates Ferratum under its Non-Bank Financial Institutions Rating Criteria as the company's main business is focused on niche consumer lending (with its banking operations mainly geared towards deposit gathering and the facilitation of lending activities on the group in select markets).

Ferratum's business model hinges predominantly on the extension of credit to customers falling outside the scope of traditional bank offerings (largely individuals but more recently also SMEs), charging a significant interest premium to compensate for the arising elevated credit risk.

The recent adoption of regulatory caps on allowable interest and fee rates in some of Ferratum's core markets (most notably in Finland, Sweden, and Latvia) has only had a moderate impact on its competitiveness in this sector, as its fairly lean cost structure and broad geographic coverage have allowed the company to reposition itself in the evolving environment. However, Fitch's company profile assessment remains weighed down by the inherent risk of regulatory intervention in this sector.

Ferratum operates in a market segment characterised by a heightened risk appetite and consequently asset quality is inherently weaker than that of traditional commercial banks (with the Stage 3 loan ratio equating to 39.6% as of end-3Q19). The adoption of IFRS 9 in 2019 (particularly impacting loan provisions) as well as the company's proactive approach to asset quality management (in particular the disposal of non-performing portfolios early in the loan life cycle) supports Fitch's expectation of a gradual improvement in key asset quality metrics, albeit at the cost of some transitory margin easing. In addition, we view risk provisioning as adequate, with the impaired loan coverage registering above 80% in 2019.

Ferratum has demonstrated an appropriate profitability track record in recent years and Fitch views margin levels as sound in the context of Ferratum's business model. In this regard, we note the recently undertaken operational improvements and efficiency enhancements, which collectively helped to absorb some of the margin lag arising from the recent adoption of IFRS 9 (and in particular associated more prudent provisioning requirements). We further note the company's intentions to increasingly act as a finance intermediary over the medium to long term, thereby focusing on loan origination while limiting own balance sheet exposure.

Ferratum has a largely unsecured funding profile, mainly comprising bank deposits (EUR205 million as of end-3Q19) and senior unsecured bonds (EUR220 million). While the bonds have long-term maturities (three to four years), online deposits are mostly shorter-term, with 89% expiring within the next three months (as of end-3Q19). In our view, these are less sticky than traditional retail deposits (particularly in periods of market stress). However, the company has some discretion with rate setting, which supports liquidity management.

We consider overall funding flexibility also in the context of regulatory constraints on moving its deposit funding within the group, particularly a requirement of equity and non-deposit funding accounting for at least 35% of deposits. Ferratum maintains a sizeable cash balance (EUR134 million as of end-3Q19), which is predominantly with the Central Bank of Malta for regulatory reasons to support its liquidity.

Overall, we consider the consolidation of Ferratum Bank in the wider company as moderately credit-positive, with an efficient market and funding access via retail deposits balancing the need for bank regulatory compliance (both with regard to capital and liquidity management).

Fitch calculates Ferratum's gross debt/tangible equity ratio as of end-3Q19 at around 5.4x, which was moderately higher than the company's historical leverage ratio of around 4x. This increase was mainly driven by two bond issuances of EUR180 million by Ferratum Capital in the past two years 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.

Senior Notes

Ferratum Capital Germany's senior unsecured bond is rated in line with Ferratum's Long-Term IDR because Ferratum acts as the guarantor of the bond issuance. The rating alignment reflects Fitch's expectation of average recovery prospects of the senior unsecured bond. The bond constitutes a direct and unsecured senior obligation of Ferratum Capital Germany and ranks *pari passu* with all present and future senior unsecured obligations of the issuer.

RATING SENSITIVITIES

IDR

A notable increase in leverage measured as debt to tangible equity above 6x could lead to a downgrade, while materially lower leverage on a sustained basis, if combined with an enhanced and more resilient franchise, could support positive rating action.

A weaker franchise, arising from a sustained loss in revenue/operational losses, an adverse reputational event, or a significant tightening of regulatory requirements in key markets resulting in a significant loss of business and/or notable margin pressure could result in a downgrade. A strengthening in franchise via improved scale and pricing power without a marked increase in risk appetite, could be rating-positive.

Increased risk appetite leading to higher credit losses as the product mix evolves toward larger and longer-term origination (such as SME loans), notably if combined with looser provisioning standards, pressuring profitability

and ultimately eroding Ferratum's capital base, would be negative for the ratings.

Signs of funding weakness in the form of a loss of retail deposits at Ferratum Bank or a loss of wholesale funding market access leading to higher refinancing risk could be rating-negative. Furthermore, any sustained adverse operational developments at the 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.

The growth of Ferratum Bank in comparison with the rest of the group leading to increased structural subordination risk for wholesale creditors outside the bank could also be rating negative.

Senior Notes

The senior notes' rating is primarily sensitive to changes in Ferratum's Long-Term IDR. Changes to Fitch's assessment of recovery prospects for senior unsecured debt in default (e.g. the introduction of debt obligations ranking ahead of the senior unsecured debt notes) could also result in the senior unsecured notes' rating being notched below the IDR.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or to the way in which they are being managed by the entity.

Ferratum has an ESG Relevance Score of 4 for Exposure to Social Impacts as a result of its exposure to the high-cost consumer lending sector and the increasing levels of regulatory scrutiny, including tightening of interest rate caps. The evolving regulatory environment has had direct impact on Ferratum's business model including the pricing strategy, product mix, and targeted customer base.

For more information on our ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING		PRIOR
Ferratum Oyj	LT IDR BB- ● Affirmed		BB- ●
Ferratum Capital Germany GmbH			
senior unsecured	LT BB- Affirmed		BB-

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Applicable Criteria

Non-Bank Financial Institutions Rating Criteria (pub. 28 Feb 2020)
Short-Term Ratings Criteria (pub. 06 Mar 2020)

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Solicitation Status
Endorsement Policy

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