FitchRatings

Fitch Downgrades 3 Turkish Independent NBFIs

Fitch Ratings-London-12 September 2018: Fitch Ratings has downgraded three Turkish non-bank financial institutions' (NBFIs) National Long-Term Ratings - Tacirler Yatirim Menkul Degerler A.S. to 'A(tur)' from 'A+(tur)', Kapital Faktoring A.S. to 'A-(tur)' from 'A+(tur)' and Destek Faktoring A.S. to 'A-(tur)' from 'A+(tur)'. The Outlooks on Tacirler's and Kapital's ratings are Negative. Destek's rating has been placed on Rating Watch Negative (RWN).

KEY RATING DRIVERS
The downgrades reflect increased risks to the companies' credit profiles following the recent period of market volatility in Turkey's operating environment. The downgrades also reflect increased risks to the companies' funding and liquidity profiles in light of their wholesale funding reliance.

The ratings are underpinned at their current levels by the companies' positions as leading independent players in the factoring (Destek and Kapital) and investment services (Tacirler) sectors as well as by their solid financial metrics, particularly modest leverage.

Independent NBFI companies' funding access has weakened in recent months, increasing liquidity pressure and refinancing risk. However, the companies under review benefit from a short-term asset base, providing them with flexibility to swiftly deleverage their balance sheets, if needed.

Kapital and Destek are among the largest non-bank owned factoring companies in Turkey by domestic factoring receivables, and have a track record of sound financial metrics. In absolute terms, however, both are small relative to Turkey's financial sector.

Both companies are exposed to a material refinancing risk due to recent market turbulence. It is mitigated by their low leverage and the short tenor of factoring receivables. Compared with Kapital, Destek's liquidity position is more dependent on market access given the longer maturities of Destek's receivables book and greater use of short-term funding.

Factoring receivables made up 98% of Kapital's and 99% of Destek's total assets at end-1H18, reflecting a monoline business model. Kapital mainly targets the SME and micro-commercial customer segments, while Destek targets mid-sized commercial borrowers. Fitch believes these customer segments are more susceptible to downturns in the Turkish economic environment, in particular in light of the weaker growth outlook.

Credit losses to date have been limited and the impaired receivables ratio (overdue by 90+ days) was a low 0.5% for Destek and 2% for Kapital at end-1H18. Short tenor assets mean that asset quality problems could rapidly manifest themselves in the financials. Fitch expects cost of risk to rise, putting pressure on profitability in 2H18-2019.

Both companies operate with high capital ratios (equity/assets of 34% for Kapital and 30% for Destek at end-1H18). Their capital position is supported by strong internal capital generation (17%for Kapital and 27% for Destek in 1H18 on an annualised basis). This provides the companies with a good buffer to absorb potential credit losses up to 32% and 28% of their respective factoring books as of end-1H18, before they breach the regulatory minimum (3% equity-to-assets). Potential shrinking of the factoring books in the near term would also underpin capitalisation.

Tacirler Investment's main business lines are margin lending and brokerage services. Retail customers were historically its core clientele, but since 2014 the company has been diversifying and targeting the corporate segment and investment banking services.

Tacirler Investment has solid capitalisation, with a 40% equity-to-assets ratio at end-1H18. This is sufficient to cover for impairment up to 49% of investments and loans combined. Fitch deems current leverage as strong for the rating, but any sustained weakening would place pressure on the ratings. Tacirler's internal capital generation improved in 1H18 to a reasonable 10% (annualised) despite low leverage.

Tacirler Investment improved its performance in 1H18 due to higher interest yield. Revenue sources remained well-diversified by type. Cost efficiency, stemming from a low cost base, supports profitability.

RATING SENSITIVITIES

The companies' ratings may be downgraded in case of constraints in refinancing, sizable losses, erosion in solvency or a notable weakening of franchise due to shrinking business volume. Further deterioration in the Turkish operating environment would also be negative for the ratings.

Kapital and Destek have significant dependence on funding from Takasbank, while it is less so for Tacirler. These are usually short-term (one-to-three months) borrowings backed by guarantee from local banks. As smooth access to Takasbank funding is key to the NBFI sector prolonged loss of access without alternative arrangements being put in place would lead to a downgrade of Kapital and Destek.

The RWN on Destek's rating reflects Fitch's view that in the current challenging operating environment refinancing risk for the company has materially increased in the short-term. While Destek is in the process of rebalancing its funding profile, it remains more sensitive than Kapital and Destek to an increase of delinquencies in its receivables book and the continued availability of bank guarantees to access Takasbank funding.

In resolving the RWN, Fitch will consider the company's ability to preserve adequate market access via bank and Takasbank funding, short-term trends in asset quality affecting cash flows and the development of the company's liquidity buffer. If Destek demonstrates an ability to lengthen its funding profile and strengthen overall liquidity, Fitch may affirm the rating and assign it a Negative Outlook, similar to the other companies.

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Applicable Criteria

National Scale Ratings Criteria (pub. 18 Jul 2018) (https://www.fitchratings.com/site/re/10038626)
Non-Bank Financial Institutions Rating Criteria (pub. 22 Jun 2018) (https://www.fitchratings.com/site/re/10034715)

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