Lider Faktoring A.S.

Key Rating Drivers

Standalone Strength Drives Rating: Lider Faktoring A.S.'s National Long-Term Rating reflects its position as an established, independent factoring company in Turkey and its record of adapting to changing economic conditions. Lider's rating also factors in a higher leverage appetite than its domestic peers and moderate scale within a highly competitive factoring sector dominated by bank subsidiaries.

Stable National Rating: National scale ratings are an opinion of creditworthiness relative to the universe of issuers and issues within a single country. The Stable Outlook reflects that Lider's credit strength remains resilient compared with its peers in Turkey.

Independent Factoring Company: Lider had a 3% market share in the domestic factoring sector at end-2019, factoring exclusively domestic local-currency receivables of Turkish SMEs. Lider is smaller than bank-owned competitors, but the industry is fragmented, which allows smaller companies to operate adequately in their niches. Lider fully consolidates Denge Asset Management Company, a bad-debt purchaser with an estimated 3% market share in domestic debt purchasing (accounting for 10% of Lider's assets at end-2019).

Pandemic Further Reduces Origination: Lider's balance sheet at end-1H20 remains below its 1H18 peak, due to successive economic crises and persistent volatility. Fitch Ratings expects growth to be muted in the short term, due to Lider's cautious credit underwriting and increased competition from banks. High credit supply at lower rates by banks discourages the use of more expensive funding sources, like factoring, but also allows de-risking the portfolio, as Lider can focus on retaining its most creditworthy clients.

Deleveraging in Challenging Environment: Balance-sheet shrinkage has supported Lider's capitalisation since 1H18. Its gross debt/tangible equity ratio improved to 5.1x at end-1H20 and we do not expect leverage to significantly increase in the short term, despite appetite for higher leverage in the medium to long term.

Adequate Profitability, Asset Quality: Fitch expects narrower margins and a modest portfolio reduction to put pressure on Lider's earnings in 2020 (net interest margin at 5% in 2019), but within our tolerance for the current rating. Impaired receivables were stable at 3.2% at end-1H20 and are fully provisioned for. Selective client retention should contain the generation of impaired receivables.

Liquid, Fast-Amortising Receivables Book: Lider's short-term balance sheet and the absence of maturity mismatches between assets and liabilities largely mitigate refinancing risk. Lider has a diversified funding base across local banks, central clearing house Istanbul Takas ve Saklama Bankasi A.S. (Takasbank) and domestic bonds. All funding is in Turkish lira, as is the receivables portfolio.

Rating Sensitivities

Limited Upside Potential: An upgrade could stem from lower leverage and a reduction in business volatility, combined with a stronger franchise and scale than domestic peers.

High Leverage, Credit Losses: Higher risk appetite (e.g. foreign-exchange or non-recourse factoring), material credit losses, leverage sustained at a higher level, refinancing difficulties or liquidity constraints could lead to a downgrade.

Ratings

National	
National Long-Term Rating	BBB(tur)
Sovereign Risk	
Long-Term Foreign-Currency IDR	BB-
Long-Term Local-Currency IDR	BB-
Country Ceiling	BB-

Outlooks

National Long-Term Rating	Stable
Sovereign Long-Term Foreign-Currency IDR	Negative
Sovereign Long-Term Local-Currency IDR	Negative

Applicable Criteria

Non-Bank Financial Institutions Rating Criteria (February 2020)

Related Research

Fitch Affirms Lider Faktoring at 'BBB(tur)'; Outlook Stable (August 2020)

Turkish Factoring Sector Dashboard: 1Q20 (June 2020)

Fitch Revises Outlook on Turkey to Negative; Affirms at 'BB-' (August 2020)

External Pressures Remain Turkey's Main Credit Weakness (July 2020)

Coronavirus Impact Will Test EMEA NBFIs' Business Models (March 2020)

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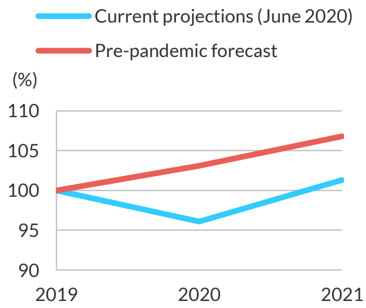
Significant Changes

Pandemic Exacerbates Existing Vulnerabilities

Fitch forecasts Turkey's GDP to contract by 3.9% in 2020 due to the coronavirus pandemic, with growth of 5.4% in 2021 (i.e. GDP in 2021 to be 1.3 percentage points higher than in 2019, compared to our projection at end-2019 of 6.8pp higher). Lockdown measures and travel restrictions have severely affected the Turkish tourism industry (accounting for 11% of GDP in 2019), with tourist arrivals in 1H20 down 75% from 1H19.

A policy-driven higher credit supply should support the recovery in 2021 and 2022. However, this and lower tourism receipts, together with previous sharp interest rates cuts (down to 8.25% in May 2020 from a peak of 24% in 2018) and increasing geopolitical risks, are renewing pressure on the lira, which depreciated by 25% between end-2019 and mid-August 2020. In our view, negative real interest rates and worsening external imbalances will keep pressure on the lira until end-2021 at least, despite the resumption of tourism in August 2020 and the tightening of offshore and onshore lira trading. Fitch has consequently revised the Outlook on Turkey's Long-Term Issuer Default Ratings (BB-) to Negative from Stable on 21 August 2020.

GDP Forecast for Turkey



Source: Fitch Ratings

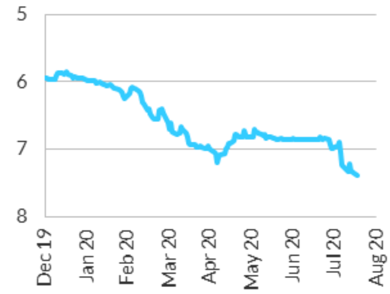
Company Profile

Medium-sized Independent Factoring Company

Lider is a medium-sized factoring company in Turkey, discounting only domestic receivables with recourse and in local currency. Lider caters to Turkish SMEs (about 3,000 clients at end-1H20) through a network of 21 branches. The majority of Lider's factoring derives from small transactions to companies enganged in manufacturing and construction.

Lider is active also in bad debt acquisition and collection through its subsidiary Denge Asset Management Company, but we expect this to remain a minor profit contributor in the medium term. Turkey's largest two bad-debt purchasers amount to over half of the industry and we do not expect banks to sell significant amounts of impaired loans in the next 12 months to avoid the crystallisation of losses.

Turkish Lira Depreciates Against US Dollar



Source: Fitch Ratings, Bloomberg

Qualitative Assessment

Operating Environment

Limited Regulation for Factoring Companies

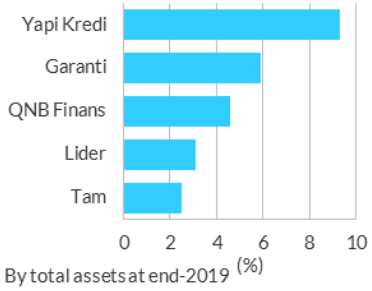
The regulatory framework for the leasing and factoring sectors in Turkey is weaker than that for banks and investment firms, which are regulated respectively by the Banking Regulation and Supervision Agency (BRSA) and the Capital Markets Board. Leasing and factoring companies are less closely monitored by the BRSA, but the regulator indirectly monitors bank-owned factoring companies as part of their parents' consolidated financial statements.

Fragmented Factoring Industry

Factoring penetration in Turkey is about half the rate in the EU (factoring transactions in Turkey and the EU were 4.9% and 9.7% of GDP in 2018, respectively), indicating growth potential. The factoring sector represented about 1% of total banking sector assets at end-2019 and is fragmented among 56, mostly small, companies. Transparency has improved since 2014 with the establishment of a central invoice registry, in which all invoices and cheques issued in Turkey must be registered.

Turkish factoring companies have a low exposure to foreign currency (less than 20% of gross receivables are denominated in foreign currency). However, a reliance on wholesale, often short-term funding highlights liquidity risks. Factoring firms are active users of the local bond market with short-term debt (up to 18 months, but usually not longer than six months), besides sourcing credit from Takasbank under bank guarantees.

Market Share of Fitch-rated Turkish Factoring Companies



By total assets at end-2019
Source: Fitch Ratings, BRSA

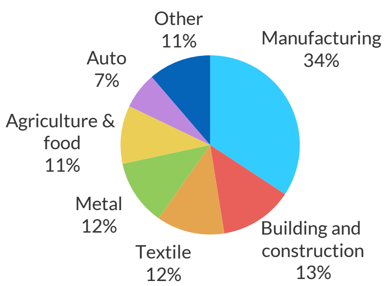
Management & Strategy

Sound Management Team

Lider's management is sound and has sufficient skills and experience. Turnover is very low and the chief executive has been in his role since 2002. The management team consist of six members and there is limited key-person risk in relation to the chief executive, given Lider's size and the absence of a parent bank that could provide a wider pool of managerial talent.

Lider plans to maintain its market share, limit credit risk and improve capitalisation. Growth plans are modest and seek to maintain market share amid price competition from banks and to select the best credit risk. Strategic objectives are consistently delivered.

Lider's Portfolio by Industry



At end-1H20
Source: Fitch Ratings, Lider

Public Listing Supports Corporate Governance

Lider is majority-owned by six private individuals who hold about 85% of the shares with its remaining shares listed on the domestic stock exchange. However, corporate governance is stronger than at other rated family businesses thanks to the adherence to Borsa Istanbul's standards. Lider has a seven-members board of directors, including two independent directors and three board committees. Share trades in 1H20 did not meaningfully alter the ownership structure.

Risk Appetite

Prudent Underwriting, Cautious Growth

Lider has a conservative risk appetite, discounting only domestic receivables, denominated in liras and with recourse. Underwriting is centralised in Istanbul, ensuring consistency across the portfolio, but local branches can reject applicants in a first vetting step. Industry exposure is reviewed through the cycle to minimise credit risk.

Portfolio growth is very volatile, thanks to the quick amortisation of receivables and Lider's opportunistic expansion. Lider has contracted materially since its peak in 2Q18 to meet lower demand and higher credit risk. Lider had aggressively expanded until early 2018 and would do so again under favourable conditions, in Fitch's view. However, we expect lending volumes to be subdued well into 2021 due to the current crisis and to strong competition from banks.

Financial Metrics

Asset Quality

Proactive Client Retention Mitigates Impaired Loans Origination

Fitch expects Lider's impaired loans to increase, but only moderately, in the next twelve months. Lider's clients are SMEs, that have limited access to bank finance or larger bank-owned factoring companies. However, this has partly changed due to the higher credit supply. In this context, Lider focused on retaining its most creditworthy clients, which allowed it to keep its impaired loans flat (TRY29 million at end-1H20). Provision coverage is solid (99% on average) and guarantees cover 110% of its portfolio (customer cheques and customer notes).

Earnings & Profitability

Own Network, Lower Rates Weigh on Profitability

Lider's operational efficiency (cost/income ratio of 78% in 1H20) is about double the industry average (30%-40% in recent years) which weighs on our assessment of its profitability. Lider caters to the labour-intensive SME segment and relies on its own branch network, while bank-owned factoring companies originate most of their business through their parent banks' franchises.

Fitch believes Lider's revenue will be under pressure in the short term, due to policy-driven low interest rates and high credit supply. Return on assets and net interest margin have halved in 1H20 and impairment charges may further weaken them in 2H20. Recoveries from the acquired non-performing loan portfolio support revenue, but still represent a small share of revenue (TRY37 million in 2019).

Capitalisation and Leverage

Low Business Origination Drives Deleveraging, but Leverage Appetite Remains

Fitch expects leverage to remain close to its end-1H20 value (debt to tangible equity of 5.1x) in the short term, due to limited business opportunities in the current environment and because of the planned dividend retention (at least until end-2020). However, we take into account Lider's opportunistic growth in the past and we do not exclude that Lider would re-lever in the medium term, after the end of the pandemic. Leverage is now significantly below its last peak (9.8x at end-1H18), when Lider temporarily breached its internal capitalisation target of 10% equity to assets.

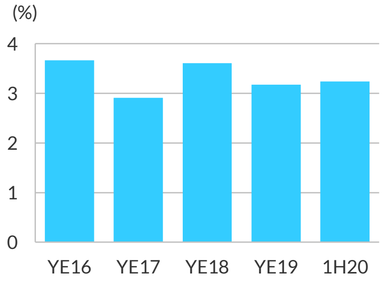
Funding, Liquidity and Coverage

Fast-Amortising Book Mitigates Short-Term, Wholesale Funding

In Fitch's view, Lider's short-dated funding profile (87% of funding is due within 90 days) is broadly aligned with the short cycle of its assets (about 110 days). Lider's funding is sufficiently diversified between unsecured bank loans (70% of total funding at end-1H20 from 13 banks), Takasbank (19%) and domestic bonds issued (11%). Lider has kept access to banks through the crisis and we do not expect lower access to funding in the medium term, although lower business origination will likely reduce the need for non-bank sources such as bonds.

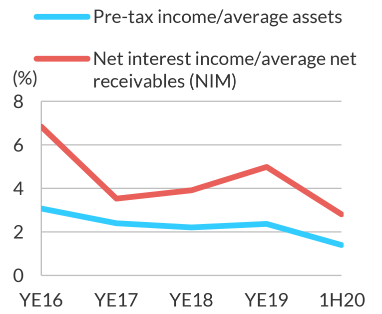
Asset Quality

Impaired receivables/gross receviables



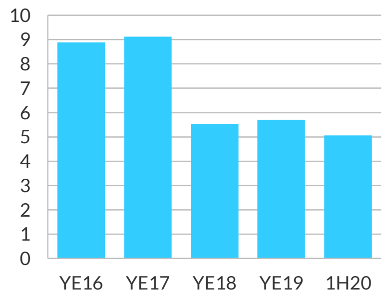
Source: Fitch Ratings

Earnings & Profitability



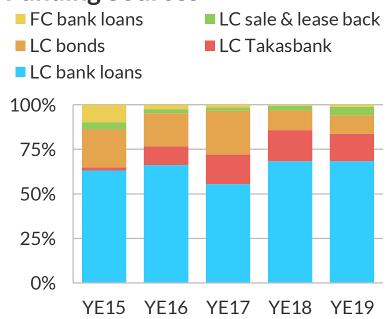
Source: Fitch Ratings

Debt/Tangible Equity (x)



Source: Fitch Ratings

Funding Sources



Source: Fitch Ratings

Income Statement

(TRYm)	2014	2015	2016	2017	2018	2019	1H20
Revenue							
Interest income	109	114	144	184	292	205	73
Other income	13	12	8	36	47	37	21
Total revenue	**123**	**126**	**152**	**220**	**339**	**242**	**94**
Expenses							
Interest expense	74	79	92	149	255	162	60
SG&A expenses	31	27	29	43	54	50	27
Impairment charges	8	11	4	-1	4	5	0
Total expenses	**113**	**118**	**125**	**191**	**314**	**217**	**86**
Pre-tax income	**9**	**8**	**27**	**28**	**25**	**25**	**8**
Income tax	2	1	5	5	5	7	1
Net income	**7**	**6**	**21**	**23**	**20**	**18**	**7**

Source: Fitch Ratings, Fitch Solutions, Lider Faktoring A.S.

Balance Sheet

(TRYm)	2014	2015	2016	2017	2018	2019	1H20
Assets							
Cash & equivalents	0	1	8	9	23	11	16
Gross receivables	**812**	**646**	**934**	**1,141**	**804**	**964**	**897**
Memo: Impaired receivables included above	20	32	34	33	29	31	29
Less: Receivable loss allowances	20	30	34	33	29	29	29
Net receivables	**793**	**616**	**900**	**1,108**	**775**	**935**	**868**
Goodwill and intangible assets	0	0	0	1	1	0	0
Deferred tax assets	4	5	6	6	5	5	2
Fixed assets	25	28	33	38	69	60	67
Other assets	17	15	124	135	123	123	120
Total assets	**839**	**665**	**1,072**	**1,297**	**996**	**1,135**	**1,073**
Liabilities							
Short-term debt	601	510	894	1,120	810	938	883
Long-term debt	102	53	55	33	18	13	0
Total borrowings	**704**	**564**	**948**	**1,152**	**828**	**951**	**883**
Deferred tax liabilities	0	0	1	1	0	2	0
Other liabilities	28	9	10	12	12	12	13
Total liabilities	**731**	**573**	**959**	**1,165**	**840**	**965**	**896**
Total equity	**107**	**92**	**112**	**133**	**156**	**170**	**177**
Total liabilities and equity	**839**	**665**	**1,072**	**1,297**	**996**	**1,135**	**1,073**

Source: Fitch Ratings, Fitch Solutions, Lider Faktoring A.S.

Summary Analytics

	2014	2015	2016	2017	2018	2019	1H20
Asset-quality metrics (%)							
Impaired receivables/gross receivables	2.4	4.9	3.7	2.9	3.6	3.2	3.2
Receivable loss allowances/impaired receivables	100.0	93.8	98.9	100.0	100.0	95.4	100.0
Impaired receivables less loss allowances/tangible equity	0.0	2.3	0.4	0.0	0.0	0.8	0.0
Receivables impairment charges/ average gross receivables	1.2	1.6	0.5	-0.1	0.4	0.5	0.0
Growth of gross receivables	34.2	-20.4	44.5	22.2	-29.6	20.0	-6.9
Impaired receivables generation	-0.2	1.7	0.3	-0.1	0.5	0.2	-0.2
Earnings and profitability metrics (%)							
Pre-tax income/average assets	1.3	1.0	3.1	2.4	2.2	2.4	1.4
Pre-tax income/average equity	9.0	7.8	26.1	23.2	17.5	15.5	8.9
Net income/average assets	1.0	0.8	2.5	1.9	1.7	1.7	1.2
Net income/average equity	7.2	6.4	20.9	18.7	13.7	11.2	7.9
Operating expenses/operating revenue	63.7	59.0	48.8	60.9	64.8	62.7	77.9
Impairment charges/pre-impairment operating profit	47.3	59.3	13.4	-2.5	14.2	15.2	-4.7
Interest income/average gross receivables	15.4	15.6	18.2	17.7	30.0	23.2	15.6
Interest expense/average debt	12.5	12.5	12.1	14.2	25.8	18.2	13.1
Net interest income/average net receivables (NIM)	5.0	4.9	6.8	3.5	3.9	5.0	2.8
Risk-adjusted NIM	3.8	3.3	6.3	3.6	3.5	4.5	2.8
Capitalisation and leverage metrics							
Debt/tangible equity (x)	6.8	6.5	8.9	9.1	5.5	5.7	5.1
Tangible equity/tangible assets (%)	12.4	13.1	10.0	9.8	15.1	14.7	16.3
Equity/total assets (%)	12.8	13.8	10.5	10.2	15.6	15.0	16.5
Funding and liquidity metrics (%)							
Unsecured debt/total debt	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Short-term debt/total debt	85.5	90.5	94.2	97.2	97.9	98.7	100.0

Source: Fitch Ratings, Fitch Solutions, Lider Faktoring A.S.

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.