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Fitch Upgrades Jerrold Holdings to 'BB-'; Stable Outlook Ratings Endorsement Policy

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Fitch Ratings-London-20 March 2015: Fitch Ratings has upgraded Jerrold Holdings Limited's (JH) Long-term Issuer Default Rating (IDR) to 'BB-' from 'B+' and affirmed its Short-term IDR at 'B'. The Outlook on the Long-term IDR is Stable. Fitch has also upgraded the rating of senior unsecured notes issued by Jerrold FinCo and guaranteed by JH to 'BB-' from 'B+'.

KEY RATING DRIVERS - IDR

The upgrade takes into account the group's improved access to a more diversified investor base for its debt, which has enabled it to grow, improve the quality of its receivables book and increase its profitability. Thanks to earnings retention, capitalisation has been rising and while debt is likely to increase, it is not expected to result in a material increase in gearing.

JH's ratings reflect the significant risks arising from its relatively undiversified business model, which relies on limited funding sources. The ratings benefit from the company's modest gearing, strong capital generation and adequate risk management.

Relative to mainstream lenders, the higher arrears present in JH's loan book are a feature of its business model, particularly in relation to pre-2011 lending, but risk is monitored and managed carefully on an individual loan basis, with strong collection and recovery policies in place. Non-performing arrears (arrears > 3 months where receipts in last three months are less than 90% of contractual instalments, and excluding JH's legacy portfolio of development loans) represented 8% of receivables at end-2014, or 16% of loans originated pre-2011 and 1.75% of those since. Actual losses are low, as the company ensures that it has a solid level of security (mostly residential property) backing its loans. Collateral values have risen over the past year, reflecting general house inflation in the UK.

Risk is well remunerated with wide margins and high fees generally not affected by movements in base rates. Revenue growth relies solely on lending volumes.

Compliance and risk controls have improved with a reduction of reliance on key individuals and rising corporate governance standards. However, the company's fast growth projections over the next three years could put pressure on its operational and risk management functions, which in turn could put pressure on its ratings.

JH's funding profile has improved following the issuance of a senior bond in September 2013 and the refinancing, expansion and extension of its securitisation transaction. Nonetheless, funding is relatively undiversified and exposes JH to refinancing risk. Asset encumbrance is also high.

The rating of the Jerrold FinCo bond is equalised with JH's ratings, as it is guaranteed by the operating entities or the group and reflects the expectation of average recovery rates.

RATING SENSITIVITIES

A company with high-risk assets, a lack of product diversification, sole reliance on wholesale funding and modest business scale would generally be rated below investment grade, therefore limiting future potential upgrades. However, JH's ratings could be upgraded in the event of further diversification of its funding

structure, with a more staggered maturity profile, accompanied by ongoing growth in capitalisation and improving asset quality. The ratings would also benefit from better liquidity, for example in the form of sustained larger funding headroom.

The ratings would be negatively affected by a prolonged inability to access wholesale funding markets, or by an unexpected significant rise in gearing. A downgrade could also follow rapid loan growth over the next couple of years if this would cause a significant weakening of the company's risk profile or if profitability suffers from greater conduct and compliance costs.

The rating of the senior unsecured notes is primarily sensitive to any movement in JH's Long-term IDR and may also be affected by potential changes to the capital structure and asset encumbrance.

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Applicable criteria, Global Financial Institutions Rating Criteria 31 January 2014 and Finance and Leasing Companies Criteria dated 11 December 2012 are available at www.fitchratings.com.

Applicable Criteria and Related Research:

Global Financial Institutions Rating Criteria
Finance and Leasing Companies Criteria

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