FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Together at 'BB-'; Outlook Negative

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Fitch Ratings - London - 30 Nov 2020: Fitch Ratings has affirmed Together Financial Services Limited's Long-Term Issuer Default Ratings at 'BB-', Short-Term IDR at 'B', and the senior secured notes issued by subsidiary Jerrold FinCo Plc (FinCo) and guaranteed by Together at 'BB-'.

Fitch has also affirmed the senior PIK toggle notes issued by Together's indirect holding company Bracken Midco1 PLC (Midco1) at 'B'.

The Negative Outlook reflects Fitch's view that while Together maintains a degree of headroom relative to its rating level, it remains sensitive to the ongoing weak credit environment, which could pressure its financial profile, in particular, asset quality, profitability and funding and liquidity.

KEY RATING DRIVERS

TOGETHER - IDRS AND SENIOR DEBT

Together's IDR is underpinned by its long-established franchise in providing secured credit to under-served borrowers, sound risk controls, generally healthy profitability and an increasingly diversified, albeit largely secured, funding profile. This mitigates the inherent risk involved in lending to a niche sector of non-standard UK borrowers and the associated funding and leverage needs.

Together is a privately-owned business and has a robust franchise, having been in operation for over 46 years as a provider of lending products to predominantly non-standard borrowers. It benefits from strong business relationships, for example, with brokers and mortgage packagers, which have proved vital for Together's ability to increase origination of specialist loans. The business is split between the regulated Personal Finance division and the unregulated Consumer and Commercial Finance division and products offered range from first- and second-charge mortgages, buy-to-let mortgages, bridging loans, commercial term loans and development finance. In the context of the overall UK mortgage market, Together's franchise is moderate.

Loans are secured on UK property with fairly conservative loan-to-value (LTV) ratios of generally below 60% at origination, which mitigates the riskier lending profile. Underwriting is of a more bespoke nature than mainstream mortgage providers and Together enhanced its processes and tightened lending criteria in 2020 as a result of the volatile economic climate.

The impact of the pandemic has led to Together's non-performing loan ratio (defined by IFRS 9 stage 3 loans/gross loans) deteriorating and at end-1Q21 (end-September 2020) it was 13.4% (FY20: 11.6%, FY19: 8.4%). Positively, customers who took out mortgage payment deferrals earlier in the year have now largely resumed payments. However, non-performing loans could continue to rise in 2021 once government support measures are phased out and in line with forecast economic deterioration, but the overall impact on our asset quality assessment is partly mitigated by Together's generally sound LTV ratios.

Profitability, defined by pre-tax income/average assets, has declined significantly in 2020 (FY20: 2.3%, FY19: 3.8%) but remains robust, reflecting Together's higher risk profile. The 2020 decline was largely due to an increase in the IFRS9 impairment charge, which was driven by worsening macro-economic projections as well as deteriorating asset quality. Profitability in 2020 was also affected by a customer redress provision of GBP17 million. While improving macro conditions could reverse some of the impairment provision, loan book deterioration could be lagged and could necessitate higher provisions over the outlook period, with profitability sensitive to the impairment provision modelling assumptions.

Furthermore, net interest margins have been declining due to increased competition and the reduction of higher margin legacy loans and funding costs could increase in the short to medium term. Positively, Together implemented a cost-saving exercise in 2020, which will generate around GBP9 million of cost savings per year.

Leverage, defined by gross debt to tangible equity, has remained relatively stable (FY20: 4.8x; FY19: 4.5x) and we do not expect a significant rise in 2021 as Together does not plan to grow the loan book at the same rate as recent years. When calculating Together's leverage, Fitch adds Midco1's debt to that on Together's own balance sheet, regarding it as effectively a contingent obligation of Together. Midco1 has no separate financial resources of its own with which to service it, and failure to do so would have considerable negative implications for Together's own creditworthiness. Profits are largely re-invested in the business and this somewhat mitigates the dependence on debt funding.

Together's funding profile is largely wholesale, via public and private securitisations, senior secured bonds issued by the financing arm Jerrold FinCo Plc, PIK notes issued by Bracken Midco 1 PLC as well as a revolving credit facility (RCF)of GBP71.9 million. Together has been diversifying its funding profile over recent years but the wholesale nature can leave it exposed to funding and liquidity risks in volatile markets.

In particular, the private securitisations contain a number of performance covenants and the senior secured bonds and RCF have maximum gearing ratios attached to them. In a worsening credit environment, these facility restrictions could limit funding availability. Positively, Together has been building up cash buffers by limiting the amount of new lending while generating a sound level of loan redemptions in line with pre-pandemic levels and unrestricted cash was GBP113 million for FY20 (FY19: GBP23 million). Together's total accessible liquidity, which includes liquidity that can be accessed from the private securitisations in exchange for eligible assets as well as RCF drawings, was around GBP270 million at end-October 2020. The debt profile is staggered, which mitigates some of the refinancing risk and Together has shown an ability to access the wholesale funding markets with a RMBS issuance in July 2020 and the re-financing of the RCF in September 2020.

MIDCO1 -SENIOR PIK TOGGLE NOTES

Midco1's debt rating is notched from Together's IDR as Midco1's debt is taken into account when assessing Together's leverage, and Midco1 is totally reliant on Together to service its obligations. The notching between Together's IDR and the rating of the senior PIK toggle notes reflects Fitch's view of the likely recoveries in the event of Midco1 defaulting. While sensitive to a number of assumptions, this scenario would only be likely to occur in a situation where Together was also in a much weakened financial condition, as otherwise its upstreaming of dividends for Midco1 debt service would have been maintained.

RATING SENSITIVITIES

TOGETHER - IDRS AND SENIOR DEBT

As reflected in the Negative Outlook, Together's IDR and debt ratings are primarily sensitive to the weak economic conditions leading to pressure on Together's asset quality, profitability or liquidity position.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

-The Outlook on Together's Long-Term IDR and debt ratings could be revised to Stable if the group's liquidity position remains resilient and the downside risks emanating from the current operating environment begin to abate, assuming other financial metrics remain broadly unchanged (or improve).

-Contained increases in arrears and unchanged franchise strength while being able to maintain adequate earnings and leverage would also support a revision of the Outlook to Stable.

-In the medium term, an upgrade would require more stable economic conditions supported by evidence that Together's franchise and business model has remained robust, in addition to improving financial-profile metrics, notably asset quality and earnings and profitability.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

-Material asset quality weakness feeding into liquidity pressures. This could arise from a significant decline in redemptions and repayments and/or material depletion of Together's immediately accessible liquidity buffer, for example if Together needs to swap eligible assets into the securitisation vehicles to cure covenant breaches driven by asset quality deterioration, then this could weaken its corporate liquidity.

- Evidence that Together's access to the wholesale funding market is restricted or on materially worse terms.

-Evidence that Together's franchise has become negatively affected by the decision to limit loan book growth.

-A material slowdown in Together's rate of internal capital generation, for example due to a deteriorating operating environment adversely affecting asset quality and leading to higher non-performing loan metrics, significant net interest margin erosion or property price declines leading to an inability to realise sufficient collateral values, could lead to a downgrade.

- Consolidated leverage materially increasing above 5x on a sustained basis, which could arise if further debt is drawn, tangible equity reduced and significant losses absorbed.

MIDCO1 - SENIOR PIK TOGGLE NOTES

The rating of the senior PIK toggle notes is sensitive to changes in Together's IDR, from which it is notched, as well as to Fitch's assumptions regarding recoveries in a default. Lower asset encumbrance by senior secured creditors could lead to higher recovery assumptions and therefore narrower notching from Together's IDR. The notes would be sensitive to wider notching if they are further structurally subordinated by the introduction of more senior notes at Midco1 with similar recovery assumptions.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit [https://www.fitchratings.com/site/re/10111579]

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

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 the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Jerrold Finco Plc					
• senior secured	LT	BB-	Affirmed		BB-
Together Financial Services Limited	LT IDR	BB- Rating Outlook Negative	Affirmed		BB- Rating Outlook Negative
	ST IDR	B	Affirmed		B
Bracken Midco1 Plc					
• subordinated	LT	B	Affirmed	RR6	B

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Non-Bank Financial Institutions Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Bracken Midco1 Plc	EU Issued
Jerrold Finco Plc	EU Issued
Together Financial Services Limited	EU Issued

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Non-Bank Financial Institutions Europe United Kingdom