Fitch Ratings

JSC TBC Leasing

Non-Bank Financial Institutions
Finance & Leasing Companies
Georgia

Key Rating Drivers

Support Drives IDRs: JSC TBC Leasing's (TBCL) Issuer Default Ratings (IDRs) are driven by the support from its parent, TBC Bank (BB-/Negative). Fitch Ratings believes that the propensity and the ability of TBC Bank, Georgia's largest bank, to support TBCL are high. This reflects the high reputational implications of a subsidiary default, as well as full ownership, the size, integration, common branding and a record of capital and funding support. TBCL is the market leader in leasing and caters to a risky segment of clients, but has collateral available.

Reputational Risk Drives Support: TBCL's foreign lenders are the same International Financial Institutions (IFIs) and impact investors from which TBC Bank sources about 60% of its own wholesale funding. Fitch believes a failure to support TBCL would significantly damage the reputation of TBC Bank with its key wholesale lenders, undermining its business model and growth potential.

Extensive Record of Support: TBC Bank has provided both capital and funding over the years to support TBCL's growth and ensure TBCL's compliance with its loans' covenants. TBC Bank injected new equity of GEL6 million in December 2019 and, at the same time, approved an additional injection in the amount of GEL2.5 million, to be disbursed in 2020 based on TBCL's needs. TBC Bank provides TBCL subordinated and senior loans as well as letters of support to enable third-party borrowing. It also facilitates TBCL's bond placements.

Closer Integration: TBCL operates in Georgia, the group's domestic market, and its role in TBC Bank's products offering is increasing, following recent regulatory changes. Being 100% owned by TBC Bank, TBCL aligns its strategy and risk policies to those of the parent, while retaining a certain operational independence. TBCL shares TBC Bank's brand and is increasingly generating new leases through the parent's branches and client referral. Funding is largely coordinated by the parent for the whole group.

Weaker Standalone Profile: TBCL's standalone profile is constrained by its leverage, as well as by its monoline business model, a weaker asset quality and a relatively high risk appetite. Leverage remained high 7.4x after the capital injection in 2019. The risk appetite, particularly in respect to credit and FX risks, is reflected in weak asset quality indicators (impaired exposures were 14.5% of the total at end-2018), but is mitigated by sound profitability above TBC Bank's own targets.

Secured Debt Equalised to IDR: TBCL's senior secured debt rating is equalised with the company's Long-Term IDR, notwithstanding the bond's secured nature and an outstanding buffer of contractually subordinated debt. This reflects high uncertainty on asset recoveries in a scenario where TBCL and TBC Bank were in default, a scenario which would likely be accompanied by considerable macroeconomic stress in the country.

Rating Sensitivities

Parent's Rating: TBCL's negative outlook mirrors that of TBC Bank and its ratings would reflect changes in the bank's ratings.

Support Is Key: A material weakening of TBC Bank's propensity or ability to support TBCL might result in a notching differential from the parent. This could be driven by the weak performance of TBCL, a greater risk of regulatory restrictions on support, or a diminishing of TBCL's strategic importance.

Relative Ranking of Securities: Changes to TBCL's Long-Term IDR would be mirrored in the company's senior secured bond rating. The possible conversion of the bond to unsecured would not lead to a rating downgrade of the issue, provided that this is accompanied by a similar conversion of TBCL's other funding facilities.

Ratings

Foreign Currency	
Long-Term IDR	BB-
Short-Term IDR	B
Local Currency	
Long-Term IDR	BB-
Short-Term IDR	B
Support Rating	3
Sovereign Risk	
Long-Term Foreign-Currency IDR	BB
Long-Term Local-Currency IDR	BB
Country Ceiling	BBB-

Outlooks

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

Applicable Criteria

Non-Bank Financial Institutions Rating Criteria (February 2020)

Country-Specific Treatment of Recovery Ratings Criteria (February 2020)

Related Research

Fitch Revises TBC Leasing's Outlook to Negative on Similar Action to Parent (April 2020)

Fitch Revises Outlooks on 5 Georgian Banks to Negative; Maintains Stable Outlook on ProCredit (April 2020)

Fitch Rates TBC Leasing's Bond 'BB-' (March 2020)

Fitch Rates TBC Leasing at 'BB-'; Outlook Stable (January 2020)

Fitch Ratings: No Major Impact on TBC Bank from Minority Shareholders Investigation (October 2019)

Fitch Affirms Georgia at 'BB'; Outlook Stable (February 2020)

Fitch Affirms 4 Georgian Banks, Revises Outlooks on TBC and BOG to Stable (April 2019)

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Issuer Ratings

Rating level	Rating
Long-Term Foreign-Currency IDR	BB-
Short-Term Foreign-Currency IDR	B
Long-Term Local-Currency IDR	BB-
Short-Term Local-Currency IDR	B
Support Rating	3
Outlook	Negative

Source: Fitch Ratings

Debt Rating Classes

Rating level	Rating
Senior Secured Debt Rating	BB-

Source: Fitch Ratings

Fitch assigned a senior secured debt rating of 'BB-' to TBCL's GEL70 million bond issuance. The issue rating is equalised with TBCL's Long-Term Local-Currency IDR of 'BB-'. No uplift reflects the high uncertainty on asset recoveries in a scenario where TBCL and TBC Bank were in default, which would likely be accompanied by considerable macroeconomic stress in the country.

The bond issuance has a three years maturity and is denominated in local currency. It is priced on a floating base (three-month Tbilisi interbank interest rate, plus a spread). It will partially refinance existing funding from local banks. The bond will be secured with a portfolio pledge by TBCL and will rank pari passu with all other senior secured lenders.

Additional Features of the Bond

TBCL's bond includes an option to release the portfolio pledge and turn the bond into an unsecured instrument. The option is triggered if all of TBCL's bilateral secured lenders (local banks and international impact investors) agree to release the portfolio pledges they received from TBCL. In that case, bondholders would be able to either put the bond or accept a higher coupon rate for its remaining maturity.

The conversion of all secured borrowings would not lead to an issue rating downgrade, provided that negative pledge covenants hold and the relative ranking of issued securities is unchanged. Still, Fitch would assign a new Senior Unsecured Debt Rating to the issue and withdraw the Senior Secured Debt Rating.

Ratings Navigator

Institutional Support			Value
Parent IDR			BB-
Total Adjustments (notches)			+0
Institutional Support:			**BB-**
Support Factors (negative)	Equalised	1 Notch	2+ Notches
Parent ability to support and subsidiary ability to use support			
Parent/group regulation		✓	
Relative size	✓		
Country risks	✓		
Parent Propensity to Support			
Role in group		✓	
Potential for disposal		✓	
Implication of subsidiary default	✓		
Integration	✓		
Size of ownership stake	✓		
Support track record	✓		
Subsidiary performance and prospects		✓	
Branding	✓		
Legal commitments		✓	
Cross-default clauses			✓

Support Matrix Legend

Tick Colors – Influence on final IDR

- Higher influence
- Moderate influence
- Lower influence

Institutional Support Assessment

TBCL's Failure Would Jeopardise TBC Bank's Access to Funding

Fitch deems that TBC Bank has a strong propensity to support TBCL, because TBCL's failure would jeopardise TBC Bank's own access to international wholesale finance.

TBC Bank borrows about 60% of its wholesale funding from IFIs and other impact investors. These provide long-term, subordinated and GEL-denominated funding, which is necessary for TBC Bank's business model due to its structurally high net-loans-to-deposits ratio (115% at end-3Q19). They also act as anchor investors in TBC Bank's bond issuances, catalysing private sector investors, and are crucial for TBC Bank's expansion plans in Azerbaijan (Nikoil Bank) and Uzbekistan (a greenfield bank with minority equity stakes of IFC and EBRD).

IFIs and other impact investors provide 43% of TBCL's funding at end-3Q19 and have all received non-binding letters of support from TBC Bank. Fitch believes that a failure to support TBCL would significantly damage the reputation of TBC Bank with its wholesale lenders, undermining its business model and growth potential.

Long Support Record by TBC Bank

TBC Bank's past capital and funding support to TBCL has a moderate, rather than high, influence on Fitch's assessment of future support, because it was for the purposes of further growth, rather than extraordinary support after operational losses. TBCL has usually met TBC Bank's ambitious financial targets (return on average equity above 20%, growth of the lease portfolio above 30% per annum, cost of risk under 2% and cost to income ratio under 40%). A weakening in TBCL's performance may reduce its strategic importance and thus the availability of capital and funding support from TBC Bank.

Capital injections were chiefly required to ensure TBCL's compliance with its loans' covenants, as portfolio growth outpaced the internal capital generation. Most recently, TBC Bank injected GEL6 million (19% of total capital) in December 2019 and approved other GEL2.5 million for 2020, if required. Capital injections have been so far timely and in adequate volume to support compliance with financial covenants. TBCL has also an outstanding GEL2.4 million subordinated loan from TBC Bank, maturing in July 2023.

TBC Bank also provides funding to TBCL, with a USD30 million credit line (of which USD28 million was drawn in December 2019). TBCL relies on the parent to facilitate the attraction of third-party funding, through non-binding letters of support and the group's investment banking arm (TBC Kapital).

Company Summary

Dominant Market Position in Georgia's Leasing Industry

TBCL is the leader leasing company in Georgia, with a 72% of total net investement in lease at end-2018. TBCL's dominant position reflects low competition in the sector. Recent regulatory changes have increased the potential for leasing companies and are attracting new entrants, so Fitch expects TBCL to gradually decrease its share while remaining the market leader.

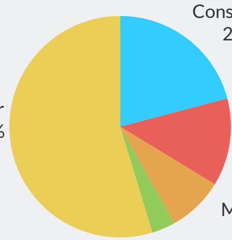
TBCL's franchise benefits from the strong brand recognition of it parent, TBC Bank, which is Georgia's largest bank (39% of system's gross loans and 39% of deposits at end-3Q19). TBCL shares its parent's brand, but until recently it operated with limited reliance on the group's resources. Fitch views positively the growing integration of TBCL in TBC Bank's MSME strategy (for Micro, Small and Medium Enterprises), which should support volume growth.

Core SME Portfolio, with Growth Plans in Retail and Real Estate

TBCL is a monoline leasing company, focusing on SMEs (legal entities represented 85% of the portfolio at end-2018) and providing financial leasing (about 95% of leasing income). TBCL's main products include automotive vehicles, construction equipment and medical equipment, but the company has recently begun to offer also real estate operational leases (such as office premises). We consider this a riskier segment but the management plans to keep a limited total exposure to real estate.

Retail leasing amounted to 15% of end-2018 portfolio. Fitch expects it to be the major growth driver in the medium term. Currently, the retail segment comprises new and used cars (respectively, 5% and 10% of the lease portfolio), but TBCL plans to introduce also consumer goods leasing as alternative to unsecured consumer loans.

Portfolio by Sector,
End-11M19



Source: Fitch Ratings

Qualitative Assessment Factors

Operating Environment

Regulatory Changes Drive Leasing Growth in Georgia

The NBG left leasing companies out of the scope of new regulation aimed at curbing fast credit growth and retail overindebtedness. Banks and microfinance organisations are instead subject to maximum loan-to-value and payment-to-income ratios, tighter underwriting requirements and higher capital requirements through risk-weighting. This new regulation increased the comparative appeal of leasing companies because they can cater to more leveraged clients. Leasing companies retain legal title of the leased assets for quick repossession and the leased assets do not count towards the lessee's total indebtedness. Fitch expects more Georgian banks and other lenders to establish leasing subsidiaries, as some have already done, increasing competition in the sector as well as its total size.

At the same time, Fitch expects that the NBG will increase its scrutiny of the leasing sector in the medium term. Prudential regulation for leasing companies is now limited to the general interest rate cap (of 50%) and to the requirement for all loans below GEL200,000 to be nominated in lari. Four leasing companies, including TBCL, have set up an industry association to manage the expected regulatory consultations.

Informal Economy, High Dollarisation and Reliance on Remittances

Georgia is a small emerging market with 3.7 million inhabitants, largely reliant on informal employment (e.g. small-scale commerce, self-employed) and remittances (12% of GDP). Growth has been robust, with Fitch estimating GDP growth of 4.3% in 2019. However, the economy is highly vulnerable to external shocks; the current account deficit narrowed in 2019, but remained at 6% of GDP, while net external debt increased to 64% of GDP. Measures capping new lending in FC have supported a decline in dollarisation to a still-high 63% of deposits and 56% of loans at end-1H19.

Georgian Lenders Pressured by Coronavirus and Oil Price Slump

The economic pressures resulting from the spread of the coronavirus and the lower oil price are credit negative for lenders in Georgia and in other CIS countries. Fitch expects a sharp economic slowdown in Georgia in 2020 (GDP contraction of 3.2%, versus growth of 5.2% in 2019), before a recovery in 2021. However, there are significant downside risks to these forecasts.

We expect that weaker economic activity will result in deteriorating asset quality, earnings and capitalisation. Weaker activity is especially expected in tourism-related sectors, together with exchange-rate pressures (the lari depreciated 16% against the US dollar between the beginning of March and 10 April, while 55% of loans were in foreign currency at end-2019) and weaker household real incomes (reflecting higher unemployment, salary reductions and decreasing remittances).

Risk Appetite

Heightened Risk Appetite, Mitigated by Collateral Availability

Fitch expects TBCL to progressively take over a riskier, but higher-yielding portion of TBC Bank's clients, thanks to its unregulated status. Fitch considers that TBCL will increase its exposure to subprime retail clients, through consumer leasing, and to residual value risk, through operational leasing of real estate and construction machinery.

TBCL has limited direct exposure to market risk, but it is highly exposed to FC-induced credit risk. Namely, TBCL is willing to issue FC leases to unhedged borrowers and about 55% of the lease portfolio is denominated in FC. TBCL also aims at issuing in FC most of the leases with original amount above GEL200,000.

Fitch believes that TBCL's collateral management and monetisation mitigates the overall high risk appetite. TBCL sets the downpayment based on the asset's liquidity and on its value depreciation on the secondary. TBCL also requires a higher downpayment for FC leases. Collateral reposession takes under a week on average.

The company has a small open FC position to tangible equity of 3% at the end-11M19.

Aggressive Growth

TBCL's rapid growth is a function of increasing leasing penetration in Georgia, though from a low base. The company was able to protect its leading market position, while its fast growth (total assets trippled in 2017-2019) has regularly outpaced the internal capital generation. The parent bank has regularly injected capital, most recently in December 2019, to support TBCL's expansion plan (at a 35% cumulative annual growth rate).

Financial Metrics

Asset Quality

High Impaired Exposures Reflect Risk Appetite

TBCL's impaired exposures were 14.5% of the total at end-2018 (the latest reported date), including both leases and other receivables under Stage 3 in IFRS9. The weak asset quality reflects TBCL's role in the group's product offering, lending to riskier borrowers on a secured basis. Fitch expects the growth in the retail segment to weigh on the asset quality in the medium term.

Reserve coverage of Stage 3 leases was modest (37% at end-11M19, 52% on average in 2015-2018), but is complemented by high collateral coverage. Adequate collateral management results in adequate impairment expenses, equal to about 2% of the average lease portfolio (2015 -2018).

Earnings & Profitability

High Risk, High Reward Model

Fitch sees positively TBCL's high profitability (return on average equity, ROAE, of 26% between 2015 and 2018), as it underpins TBCL's role in its parent's strategy. TBCL's ROAE is driven by its high portfolio yield (16.5% 2015-2018), which leaves a sound margin (5.1%) after the cost of funding, impairments and insurance expenses. Operating costs remain moderate on average, at 57% of net interest revenues (after insurance expenses). We expect profitability to remain solid in the medium term, despite pressure on corporate lending rates.

Capitalisation & Leverage

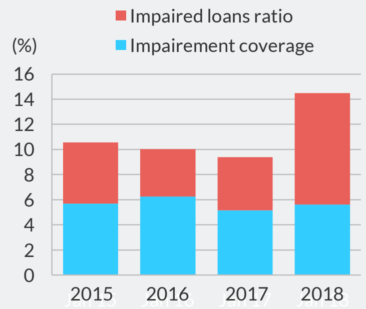
High Leverage, Capital Optimisation at Group Level

TBCL's leverage remains high (debt-to-tangible equity 7.4x) even after recent injections by the bank, especially in the context of its high risk appetite and weak asset quality. Leverage is considerably weaker than at independent peers resulting from TBC Bank's group-wide capital optimisation policy.

Fitch considers that TBCL's capital quality is further weakened by material net unreserved impaired loans (17% of end-11M19 tangible equity) and by concentration by single name (ten largest exposures at 1.7x tangible equity).

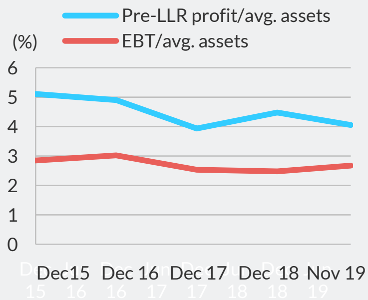
Fitch does not give equity credit to TBCL's subordinated debt of GEL32 million (9.5% of total assets at the end-11M19), because it mostly matures in January 2023.

Asset Quality



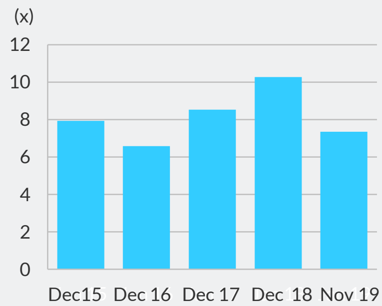
Source: Fitch Ratings

Profitability



Source: Fitch Ratings

Debt/Tangible Equity



Source: Fitch Ratings

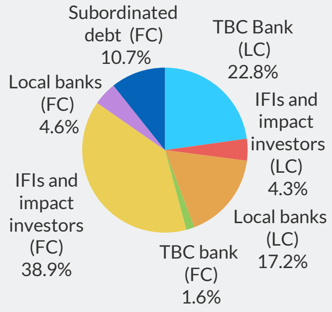
Funding, Liquidity & Coverage

Secured Funding and Support from the Parent

The majority of TBCL's funding (88% at end-2018) is secured with its lease portfolio, to guarantee pari passu across all TBCL's third-party senior lenders. In addition, NBG regulation mandates that all lending to related parties must be on a secured basis, including any lending from TBC Bank to TBCL. The latter has already obtained the necessary consent to release the collateral from most of its bilateral lenders, conditional to all outstanding lenders accepting. Fitch expects the collateral to be released in the medium term.

TBCL's access to third-party funding is driven by the support from TBC Bank. TBC Bank also provides a funding line to TBCL of USD30 million, of which only USD2 million (or 3% of total borrowings) remain undisbursed at end-2019. The line size is constrained by the regulatory requirements but we believe the NBG might waive the restriction in the event of temporary extraordinary liquidity need.

Debt Sources at End-11M19



Source: Fitch Ratings

Income Statement

(GEL 000)	Nov 19	2018	2017	2016	2015
Revenues					
Interest income	48,392	41,391	22,805	16,767	15,242
Interest expense	-18,766	-15,356	-9,345	-7,357	-6,209
Net interest income	**29,626**	**26,035**	**13,460**	**9,410**	**9,033**
Operating expenses	-16,278	-14,803	-8,977	-6,180	-4,653
Thereof: Insurance costs	n.a.	-3,476	-1,875	-1,615	-1,061
Other income, net	-763	537	1,787	1,872	875
Gain (loss) on repossessed and other assets	117	-789	71	480	-650
Impairment expenses	-5,038	-4,886	-2,256	-2,139	-2,037
Pre-tax income	**7,664**	**6,094**	**4,085**	**3,443**	**2,569**
Income tax (exempt since 2017)	0	0	0	-166	-502
Net income	**7,664**	**6,094**	**4,085**	**3,277**	**2,066**

Source: Fitch Ratings, JSC TBC Leasing

For the tables above and in the next pages, Fitch used audited IFRS financial statements for 2018, 2017, 2016 and 2015; it used unaudited IFRS management accounts for 11M19.

Balance Sheet

(GEL 000)	Nov 19	2018	2017	2016	2015
Assets					
Cash & equivalents	10,234	18,639	7,829	2,636	5,283
Due from banks & restricted cash	0	0	4,468	2,641	5,557
Net investment in lease before allowance	**n.a.**	**261,776**	**182,997**	**116,091**	**92,672**
Memo: Impaired receivables included above	n.a.	37,916	17,164	11,648	9,793
Less: loss allowances	n.a.	-14,675	-9,415	-7,255	-5,276
Net investment in lease	**301,271**	**247,101**	**173,582**	**108,836**	**87,397**
Prepayments	3,403	2,490	3,013	1,028	1,075
Goodwill and intangible assets	1,552	1,160	717	508	87
Tax assets	1,776	1,019	2,463	764	2,048
Repossessed collateral	7,862	7,805	3,328	2,573	4,463
Fixed & other assets	10,823	11,470	5,429	2,559	141
Total assets	**336,920**	**289,684**	**200,829**	**121,545**	**106,051**
Liabilities					
Advances from customers	21,344	17,726	12,907	7,044	6,699
Secured debt from financial institutions	239,535	204,369	135,782	68,236	66,056
Issue securities	0	8,094	7,798	13,261	4,798
Subordinated debt	32,056	29,247	15,685	15,834	15,073
Other liabilities	11,604	5,531	9,257	1,855	2,502
Total liabilities	**304,540**	**264,967**	**181,429**	**106,229**	**95,128**
Total equity	**32,380**	**24,717**	**19,401**	**15,316**	**10,924**
Total liabilities and equity	**336,920**	**289,684**	**200,830**	**121,545**	**106,051**

Source: Fitch Ratings, JSC TBC Leasing

Summary Analytics

(%)	Nov 19	2018	2017	2016	2015
Asset quality metrics					
Impaired receivables/net investment in lease before allowance	n.a.	14.5	9.4	10.0	10.6
Receivable loss allowances/impaired receivables	n.a.	38.7	54.9	62.3	53.9
Impaired receivables less loss allowances/tangible equity	n.a.	98.7	41.5	29.7	41.7
Receivables impairment charges/average gross receivables	n.a.	2.2	1.5	2.0	2.5
Growth of net investment in lease before allowance	12.7	43.0	57.6	25.3	32.9
Impaired receivables generation	n.a.	12.7	5.2	2.0	4.8
Lease portfolio dollarisation	55.0	66.2	75.9	90.1	87.6
Earnings and profitability metrics					
Pre-tax income/average assets	2.7	2.5	2.5	3.0	2.8
Pre-tax income/average equity	26.8	27.6	23.5	26.2	28.2
Operating expenses less insurance costs/net revenues	n.a.	46.8	57.6	48.5	39.8
Insurance costs/net revenues	n.a.	14.4	15.2	17.2	11.7
Impairment charges/pre-impairment op. profit	n.a.	44.5	35.6	38.3	44.2
Interest income/average net investment in lease before allowance	n.a.	16.8	14.3	16.1	18.8
Interest expense/average debt	n.a.	7.7	7.3	8.0	8.7
Net interest income less insurance and loss allowances/av. net investment in lease before allowance	n.a.	5.4	4.3	4.4	6.2
Capitalization and leverage metrics					
Debt/tangible equity (x)	8.8	10.3	8.5	6.6	7.9
Debt/tangible equity plus subordinated debt (x)	4.3	4.6	4.6	3.2	3.3
Tangible equity/tangible assets	n.a.	8.2	9.3	12.2	10.2
Impaired receivables less loss allowances/tangible equity	n.a.	98.7	41.5	29.7	41.7
Funding and liquidity metrics					
Unsecured debt/total debt	n.a.	12.1	9.8	16.3	17.5
Short-term debt/total debt	n.a.	48.0	41.9	26.9	29.4
Fc debt/total debt	n.a.	65.9	75.8	87.0	89.7
Liquid assets/total assets	n.a.	6.4	3.9	2.2	5.0
Aggregate maturity gap/tangible equity	n.a.	3.3	9.1	51.3	29.1

Source: Fitch Ratings, JSC TBC Leasing

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.