Credit Rating Announcement

GCR affirms TUHF Limited's BBB-$_{(ZA)}$/A3$_{(ZA)}$ long and short-term national scale ratings. Outlook Stable

Rating Action

29 July 2021 - GCR Ratings ("GCR") has affirmed TUHF Limited's national scale long and short-term issuer ratings at BBB-$_{(ZA)}$/A3$_{(ZA)}$, Outlook revised to Stable.

Rated Entity	Rating class	Rating scale	Rating	Outlook/Watch
TUHF Limited	Long Term Issuer	National	BBB-$_{(ZA)}$	Outlook Stable
	Short Term Issuer	National	A3$_{(ZA)}$	

Rating Rationale

The change of outlook to Stable, from Ratings Watch Negative, reflects the ongoing improvement in funding and liquidity after the recent completion of the Urban Ubomi (RF) Limited securitisation (R609m) that has somewhat alleviated short-term refinancing risk. The affirmation of the ratings incorporates the maintenance of sound capitalisation and improved loan collection levels (somewhat easing asset quality pressure) following the mid 2020 slump amidst the pandemic, balanced by medium term risks that could still materialise in the form of persistently higher non-performing loans ("NPLs").

TUHF predominantly focusses on providing finance to property entrepreneurs for the purchase, and/or conversion/refurbishment of buildings in the inner cities of South Africa and as such, has a niche market focus, characterised by geographic, segment and obligor concentrations. However, the relatively small size and mono-line operations are mitigated by TUHF's long standing track record operating in inner city property development and strong Environmental, Social and Governance ("ESG") credentials that were highlighted through the recently concluded securitisation, which was one of the first social bonds listed on the Johannesburg Stock Exchange and classified under the Sustainability segment. As the demand for these instruments grows, this could play a bigger role in TUHF's longer-term growth objectives by providing access to a more diverse set of lenders/funding sources and improve the cost of funding.

TUHF's capital and leverage is considered to be intermediate, and GCR believes there is adequate levels of loss absorption capacity within the capital structure that could sustain current capital metrics through the uncertain operating environment, especially given the market segments in which TUHF operates. Based on our projections, we think the GCR leverage ratio is likely to stay above 11% over the rating horizon, while GCR calculated risk weighted capital (the risk weightings are internally derived) could also be sustained around 18% in a stress scenario. Looking ahead, there is scope for earnings to improve based on strong loan growth and reduced cost of funding. However, we believe earnings may be susceptible to collateral revaluations that could see loan-to-value ratios deteriorate, and given the comparatively lower provisions, could result in higher credit losses that may impede earnings potential, and consequently limit capital build.

Asset quality has shown notable deterioration over the past few years as NPLs rose to 7.9% at FY21, from a low of 2.5% at FY18. This is balanced against well contained credit losses that have typically (except for FY20) been below 1%. Given the high concentration to the top five clients (c.29.2% of total loans) as well as the vulnerability of the target market to economic stress (middle to low income individuals), asset quality is expected to remain an area of rating sensitivity going forward as not all obligors will be able to fully recover from the impact of the pandemic and this could increase credit risk over the medium term. TUHF expects to improve the diversification of the loan portfolio by expanding into areas that border the inner city while also reducing reliance on single obligors (through large expected loan prepayments). If successful, this could partly offset some of the expected weakening in asset quality over the rating horizon, although we believe NPLs will remain elevated above 8% over the next 12-18 months.

The combined funding and liquidity assessment is negative to the ratings. Historically, TUHF has relied on short-term funding which caused significant asset/liability mismatches, leaving the entity more exposed to market closures and refinancing risk. TUHF is in the process of restructuring the funding base in order to diversify funding sources and lengthen the maturity profile of debt. To this end, TUHF recently concluded the securitisation that freed up c.R500m from a warehouse facility, with further tap issuances planned in the second half of the year. The restructuring could also see cost of funding come down to c.6.4%, from around 7.7% at FY21.

The improved liquidity position resulted in a moderation of the negative assessment. In this regard, a critical aspect to alleviating liquidity stress was the addition of fund availability under the current warehouse facility and planned finalisation of two new credit lines (combined amount of R390m, of which, a R200m credit line has been concluded). Our cash flow forecast point to short-term (less than a year) liquidity sufficiency with sources of liquidity expected to cover uses by 1x. Nonetheless, slight deviations from the underpinning assumptions, such as reduced loan book receipting, higher default rates and failure to secure or execute planned funding strategy could cause a liquidity stress and weaken TUHF's ability to meet short-term obligations on an ongoing basis. As such, we will continue to monitor the progress in strengthening the funding and liquidity structure and should this be demonstrated through the next 12-18 months, this could underpin a more stable view on liquidity.

Outlook Statement

The Stable outlook balances the improved funding and liquidity position, adequate capital and leverage viewed to be sustainable at current levels with room to absorb potential earnings volatility, against uncertainty in the operating environment that could cause asset quality deterioration. Should TUHF successfully execute its planned funding restructure through the year, TUHF could build a slight buffer in the sources of liquidity coverage over short-term liabilities, supportive of liquidity sufficiency. However, in the current operating environment, we believe rating sensitivity to asset quality deterioration could increase, and sustained weakening of NPLs and/or credit losses, coupled with higher than expected earnings volatility, could negatively impact the rating over the medium term.

Rating Triggers

Downward rating movement could arise from any signs of liquidity pressure, weaker than expected earnings that erodes existing capital buffers and further asset quality deterioration. While unlikely over the short term, upward rating movement over the medium term could stem from a demonstrated track record of improved funding and liquidity management, where sources of liquidity over short-term liabilities consistently tracks above 1x, maintaining capital and leverage at current levels or better, and improving asset quality.

Analytical Contacts

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Related Criteria and Research

Criteria for the GCR Ratings Framework, May 2019
Criteria for Rating Financial Institutions, May 2019
GCR Ratings Scale, Symbols & Definitions, May 2019
GCR Country Risk Scores, July 2021
GCR Financial Institutions Sector Risk Scores, June 2021

Ratings History

TUHF Limited					
Rating class	Review	Rating scale	Rating	Outlook	Date
Long Term Issuer	Initial	National	BBB-(ZA)	Stable	September 2013
	Last	National	BBB-(ZA)	Ratings Watch Negative	December 2020
Short Term Issuer	Initial	National	A3(ZA)	N/a	September 2013
	Last	National	A3(ZA)	N/a	December 2020

Risk Score Summary

Rating Components & Factors	Risk scores
Operating environment	**12.00**
Country risk score	7.00
Sector risk score	5.00
Business profile	**(1.50)**
Competitive position	(1.50)
Management and governance	0.00
Financial profile	**(0.50)**
Capital and Leverage	0.50
Risk	0.50
Funding and Liquidity	(1.50)
Comparative profile	**0.00**
Group support	0.00
Government support	0.00
Peer analysis	0.00
Total Score	**10.00**

Glossary

Balance Sheet	Also known as Statement of Financial Position. A statement of a company's assets and liabilities provided for the benefit of shareholders and regulators. It gives a snapshot at a specific point in time of the assets the company holds and how they have been financed.
Capital	The sum of money that is invested to generate proceeds.
Cash	Funds that can be readily spent or used to meet current obligations.
Debt	An obligation to repay a sum of money. More specifically, it is funds passed from a creditor to a debtor in exchange for interest and a commitment to repay the principal in full on a specified date or over a specified period.
Diversification	Spreading risk by constructing a portfolio that contains different exposures whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Exposure	Exposure is the amount of risk the holder of an asset or security is faced with as a consequence of holding the security or asset. For a company, its exposure may relate to a particular product class or customer grouping. Exposure may also arise from an overreliance on one source of funding. In insurance, it refers to an individual or company's vulnerability to various risks
Income	Money received, especially on a regular basis, for work or through investments.
Interest	Scheduled payments made to a creditor in return for the use of borrowed money. The size of the payments will be determined by the interest rate, the amount borrowed or principal and the duration of the loan.
Issuer	The party indebted or the person making repayments for its borrowings.
Leverage	With regard to corporate analysis, leverage (or gearing) refers to the extent to which a company is funded by debt.

Liquidity	The speed at which assets can be converted to cash. It can also refer to the ability of a company to service its debt obligations due to the presence of liquid assets such as cash and its equivalents. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Long Term Rating	See GCR Rating Scales, Symbols and Definitions.
Margin	A term whose meaning depends on the context. In the widest sense, it means the difference between two values.
Market	An assessment of the property value, with the value being compared to similar properties in the area.
Maturity	The length of time between the issue of a bond or other security and the date on which it becomes payable in full.
Rating Outlook	See GCR Rating Scales, Symbols and Definitions.
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
Short Term Rating	See GCR Rating Scales, Symbols and Definitions.
Short Term	Current; ordinarily less than one year.

Salient Points of Accorded Ratings

GCR affirms that a.) no part of the ratings were influenced by any other business activities of the credit rating agency; b.) the ratings were based solely on the merits of the rated entity, security or financial instrument being rated; and c.) such ratings were an independent evaluation of the risks and merits of the rated entity, security or financial instrument.

The credit ratings have been disclosed to TUHF Limited. The ratings above were solicited by, or on behalf of, the rated entity, and therefore, GCR has been compensated for the provision of the ratings.

TUHF Limited participated in the rating process via telephonic discussions and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible. The information used to analyse and accord the credit ratings included:

- Unaudited financial results as at 31 March 2021 (and four years of comparative numbers);
- Management budgets for 2022; and
- Other relevant information.