FitchRatings

RATING ACTION COMMENTARY

Fitch Assigns Swedish Debt Purchaser DDM 'B(EXP)' IDRs; Secured Debt 'B(EXP)'

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Fitch Ratings - Frankfurt am Main - 22 Mar 2021: Fitch Ratings has assigned DDM Holding AG (DDM) and DDM Debt AB (DDM Debt) expected Long-Term Issuer Default Ratings (IDR) of 'B(EXP)' with Stable Outlooks. At the same time, Fitch has assigned DDM Debt's planned senior secured notes a 'B(EXP)' long-term rating.

Fitch has assigned expected IDRs because we believe DDM's financial position, in particular funding, liquidity and coverage as well as growth opportunities, will be materially different after the planned bond issuance than its current position. Consequently, the assignment of final IDRs is contingent on the successful execution of DDM Debt's planned senior secured bond issuance. The assignment of final issue ratings is contingent on the receipt of final documents confirming to information already received.

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DDM is a small Switzerland-domiciled and Stockholm-listed debt purchaser with operations largely in south-eastern Europe (notably Croatia). Sweden-domiciled DDM Debt is fully-owned by DDM.

KEY RATING DRIVERS

IDR Constrained by Company Profile: DDM's expected Long-Term IDR reflects its small size (compared with rated peers). Its correspondingly more volatile performance and more concentrated business model represent constraints on its overall rating. Fitch has scored DDM's Company Profile at 'b-' and this is of High Importance to the overall rating.

Nominal Franchise; Evolving Business Model: Compared with higher-rated peers, DDM's franchise is small (120 months estimated remaining collections (ERC) of EUR258 million at end-2020, of which DDM expects to receive EUR174 million in the next three years) and concentrated by geography (Croatia accounted for 73% of ERC for the next three years at end-2020) and type (82% secured non-performing loans (NPL) based on end-2020 ERC to be received within the next three years). This represents a relatively well-defined niche franchise, but Fitch understands that DDM's business model could evolve in terms of markets and product types.

Reliance on Third-party Providers: DDM relies on third-party servicers for the collection of unsecured NPLs and uses a related company (Ax Financial Holding S.A.) for the collection of some of the secured debt. In Fitch's view, the reliance on external collection services limits the value of DDM's own franchise.

Stake in Addiko Bank: In 2020 DDM acquired a 9.9% stake in Austria-based Addiko Bank AG with the publicly stated intention to further increase its stake in the bank. There is an overlap between Addiko Bank's and DDM's strategic focus (secured lending in south-eastern Europe), but Fitch views the investment as opportunistic in the context of DDM's debt purchaser business model.

Ambitious Growth Plans: Fitch views DDM's risk controls as adequate but notes that controls will likely be stretched by ambitious growth expectations. It has an identified investment pipeline of over EUR250 million and targets to significantly grow the book in size compared with today.

Adequate but Volatile Profitability: DDM's profitability is sound, supported by a strong, albeit declining portfolio internal rate of returns and relatively moderate leverage (and associated finance expense) to date, as reflected in solid and consistent EBITDA margins and the company's ability to report moderate but consistently positive net income. However, in absolute terms, DDM's EBITDA is considerably more volatile than peers and in 2020 benefited from around EUR60 million accelerated collections due to DDM's exit from the Greek market.

In addition, DDM's overall profitability will to some extent rely on Addiko Bank's dividend payment capacity (with a projected dividend yield of 18% for 2021). Fitch notes positively that DDM has excluded the Addiko Bank dividend from its EBITDA margin calculation.

Post-transaction Leverage Acceptable: Based on management projections, DDM's cash flow leverage (gross debt/adjusted EBITDA) will increase to 3.5x at end-2021 (the lower end of Fitch's 'bb' leverage range) from 1.4x at end-2020. Positively, even under Fitch's downside scenario (which haircuts projected collections by 20% each year and keeps collection costs unchanged), DDM's deleveraging capacity is considered sound, with cash flow leverage reducing from 4.9x at end-2021 to 1.9x at end-2025. Fitch scores DDM's Capitalisation & Leverage at 'b', which reflects leverage under Fitch's base case (4.1x at end-2021), DDM's small size and concentrated risks, but also its above-average deleveraging profile.

Acceptable Liquidity; Concentrated Funding Profile: Post-transaction, DDM's liquidity position will be sound, with around EUR122 million in cash and EUR27 million draw-down capacity under its revolving credit facility (RCF). However, Fitch's Funding, Liquidity & Coverage score takes into account that DDM's cash level will quickly normalise (to around EUR16 million to EUR18 million over the business plan horizon plus EUR27 million RCF capacity) due to rapid portfolio acquisitions. The score also reflects DDM's concentrated funding profile and corresponding medium-term refinancing risk, with virtually all its post-transaction funding due in 2026.

Senior Secured Notes: The expected rating on DDM Debt's senior secured notes reflect Fitch's expectation of average recoveries, resulting in an equalisation of the bonds' ratings with DDM's Long-Term IDR. This is largely because despite their secured nature, the notes are junior to DDM's EUR27 million RCF and represent DDM's main outstanding debt.

ESG CONSIDERATIONS

Fitch assigns DDM an ESG score of '4' in relation to financial transparency, in view of the significance of internal modelling to portfolio valuations and associated metrics such as estimated remaining collections. However, this is a feature of the debt purchasing sector as a whole, and not specific to DDM.

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

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RATING SENSITIVITIES

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

Increased Size, Improved Diversification: A materially larger, more diversified franchise supporting a more stable company profile, in conjunction with maintained or improved financial metrics, could lead to an upgrade of DDM's Long-Term IDR in the medium to long term.

Senior Secured Notes: The notes' expected rating is principally sensitive to changes in DDM Debt's Long-Term IDR. In addition, improved recovery expectations, for instance as a result of a layer of more junior debt, could lead Fitch to notch up the notes' expected rating up from DDM Debt's Long-Term IDR.

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

Higher Leverage: Given its business model, DDM's cash EBITDA is more volatile than that of most of its peers, which has been factored into our assessment of Capitalisation & Leverage. However, gross leverage exceeding 4.5x on a sustained basis and, inability to de-lever in line with management projections in the medium term could put pressure on DDM's Long-Term IDR.

Tighter Liquidity: Tighter liquidity and inability to address refinancing needs in 2026 well ahead of the contractual maturity could put pressure on DDM's ratings.

Senior Secured Notes: The notes' expected rating is principally sensitive to changes in DDM Debt's Long-Term IDR. In addition, worsening recovery expectations, for instance as a result of a layer of more senior debt, could lead Fitch to notch down the notes' expected rating up from DDM Debt's Long-Term IDR.

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]

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DATE OF RELEVANT COMMITTEE

18 March 2021

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.

RATING ACTIONS

ENTITY/DEBT	RATING			RECOVERY
DDM Holding AG	LT IDR	B(EXP) Rating Outlook Stable	Expected Rating	
DDM Debt AB (publ)	LT IDR	B(EXP) Rating Outlook Stable	Expected Rating	
• senior secured	LT	B(EXP)	Expected Rating	RR4

VIEW ADDITIONAL RATING DETAILS

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Additional information is available on www.fitchratings.com

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

DDM Debt AB (publ)	EU,UK Endorsed
DDM Holding AG	EU,UK Endorsed

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https://www.fitchratings.com/site/regulatory), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

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Non-Bank Financial Institutions Europe Sweden Switzerland

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