Rating report

1 June 2019

EuroRating assigns 'BBB-' long-term credit rating to Senior Secured Fixed Rate Bonds of the company Propifi Capital Ltd (UK)

Public / Private rating	Public
Continued / One off rating	Continued (monitored rating)
Category	Rating for a bond issue
Bonds issued by	Propifi Capital Ltd (UK)
Type of the rated bonds	Senior Secured Fixed Rate Bonds (GBP)
Bonds maturity date	30 November 2024 (ISIN: GB00BJXRPX80)
Type of the credit rating	Long-term, international scale
Date of rating assignment	1 June 2019
Rating level	BBB-
Rating outlook	Stable

The presented credit rating is a rating for a bond issue and relates to the issue of up to £25 million Senior Secured Fixed Rate Bonds planned (or issued) by the company Propifi Capital Ltd ("Propifi") with its registered office in Coventry (United Kingdom), launched on 29th of April 2019, with the Final Maturity Date of 30th November 2024 (ISIN: GB00BJXRPX80). The presented credit rating does not relate to the credit risk of the issuer.

Key rating drivers

Bonds' protection by solid assets: The bonds will be secured by a first charge over property assets and personal guarantees from borrowers of Propifi. The maximum LTV rate at 70% assures an adequate protection against any adverse changes in property prices.

The bonds are legally protected in the case of Propifi's default or insolvency: The bonds' collateral will be held by an independent trustee or security company on behalf of the bond holders. This ensures that if Propifi Capital Limited defaulted or went into insolvency it would not affect the security being relied upon by the bond holders as this would be managed by the security trustee.

Moderate assets portfolio diversification: Funds from bonds will be invested in short-term bridging loans on the property market. Propifi at one time will have to invest in loans for a minimum 5 properties, which shall assure a satisfactory risk distribution.

The issuer is a new company: Propifi Capital Ltd is a start-up company, established in 2018, as a platform for peer-to-peer property loans. The issuer has no track record in investing in bridging loans on the property market at its own risk.

The issuer is characterised by an increased/high credit risk: Propifi, as a new and yet small company, with no or little track record, as a rule, is characterised by an increased credit risk. Moreover, the company has been relatively poorly equipped with equity and in the starting period generated losses

Propifi's experienced management team: Propifi has been established by a team of experienced managers with highly competent crisis management capabilities, which gives investors assurance eg. that their money will not be invested in real estate with an overestimated value, this should significantly reduce the risk of recovering money in the event of a debt collapse.

Fairly stable real estate prices in the UK: The funds will be invested in property loans only on the British market, which has been characterised by a relatively high stability. In 2007 (global financial crisis) the average UK house lost 20% of its value in the 16 months to February 2009. The Propifi loans will be secured up to 70% Loan To Value based on Open Market Valuation of the property. Even in case of similar drop in prices there should be enough equity to allow loan funds to be recouped.

Liquidity Risk: If a borrower is not able to pay back the loan, the lender must sell the property on the market. A liquidity problem in Propifi's loans portfolio may arise in case of a several property owners insolvencies in a short period of time, as the properties are usually not liquid and may not be sold quickly at acceptable prices.

Stable rating outlook

The stable outlook assigned to the rating means, that according to current estimates of the EuroRating credit rating agency the rating should most probably remain unchanged in the horizon of the next 12 months.

Factors that could lead to a rating change

Positive:

- Successful development of the basic operating activity of Propifi and generating by the company positive financial results and cashflows.
- Building by the Propifi a positive track record in granting loans at its own risk, which would result in generating profits and strengthening of the the capital position of the company.

- Better than currently expected diversification of the loans portfolio securing the bonds.

Negative:

- Having a large number of defaults in the own loans portfolio and/or generating losses on investments in loans at own risk.
- Generating by Propifi much weaker than currently forecasted income and net profits (and especially generating losses) from the operating activity.
- A further weakening of the capital position of the company.
- Keeping a low diversification of the loans portfolio.

Issuer profile

Company name: Propifi Capital Limited. **Registered office**: 5 The Quadrant, Coventry, CV1 2EL, United Kingdom. **Company registration number**: 11304890 (registered in England & Wales). **Legal Entity Identifier**: 8945006YIEQBNZEP2Q92.

Propifi is a trading name of Propifi Capital Ltd., an appointed representative of Resolution Compliance Limited, who are authorised and regulated by the Financial Conduct Authority (FRN: 574048).

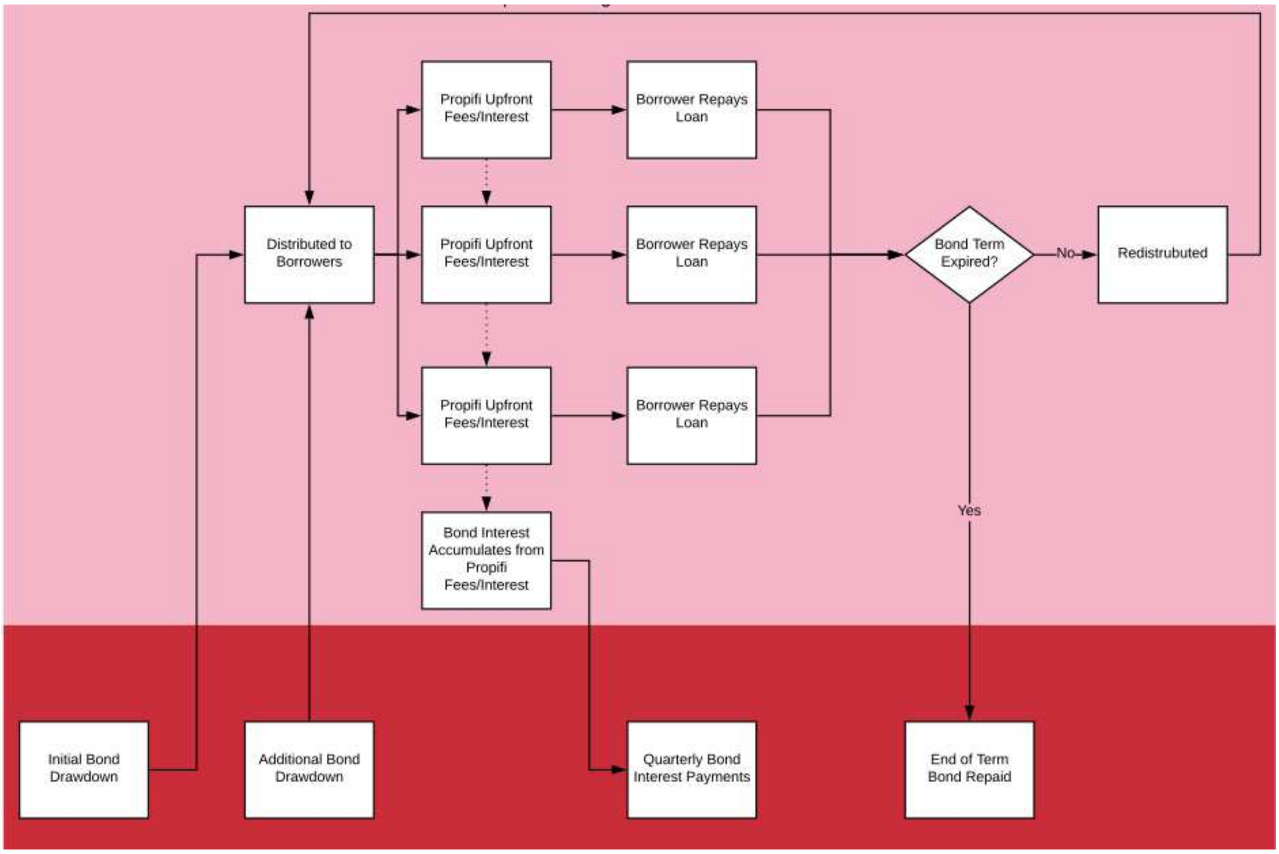
Business activity: Propifi is launching an online Peer-2-Peer property crowdfunding platform that combines leading-edge technology with an experienced team in property finance to solve the shortage of credit availability for developers and provides access to high return growth opportunities for property investors. Propifi is operating as intermediary between investors and borrowers, doing a due diligence of the properties and assessing the credit risk of the borrowers. The company plans also to invest funds at its own risk in short-term bridging property loans.

Lending and cashflow process

The loans will have first charge security in place over property/land and personal guarantees from borrowers to a minimum of 70% loan to value ratio. The security will be held by an independent trustee/security company. This ensures that if Propifi defaulted or went into insolvency it would not affect the security being relied upon by the bond holders as this would be managed by the security trustee.

The funds obtained from the bonds issue will be directly used for loans. In no case they will be used to cover the day-to-day operations of the company or otherwise.

Chart 1. Propifi Capital Ltd – lending and cashflow process



Source: Propifi Capital Limited; Bond flow, interest payments and end of term settlement.

Operating capital for Propifi is generated across a combination of upfront fees ranging from percentage-based arrangement fees, management and administration fees, and exit fees, as well as interest charges, typically annual equivalent of 18-20% across 3-12 months terms, generating positive cash flow to manage the 8.1% bond interest rate.

Description of the loans portolio

- the maximum loan value will not exceed 70% Loan To Value ratio, based on Open Market Valuation of the property
- the value of a loan will be between £100k and £5m
- the maximum loan period will be 12 months (average 3-6 months)
- Propifi will have to invest at one time in loans for a minimum 5 properties to assure a risk distribution
- loans for owner occupied real estate, working farms; sports stadiums will not be accepted.

Information on the bonds issue

The Initial Bonds issue was launched at 29th of April 2019, with the Final Maturity Date of 30th November 2024. The Propifi will pay interest, the first Payment Date shall be 8th January 2020 and the last Interest Payment Date shall be the relevant Redemption Date. The Interest Rate is 8.10 per cent per annum. The Bonds are denominated in UK Pounds Sterling.

The initial nominal amount of each Initial Bond is £100,000, and the maximum total nominal amount of the Initial Bonds is £25 million. The bonds will be offered to Institutional investors over a 5-year term. All Initial Bonds are issued on a fully paid basis at an issue price of 100% of the Initial Nominal Amount.

The bonds raised will be used to fund bridging loans in the commercial UK property market. Lending is underwritten by the experienced and FCA authorised Propifi Credit Panel. All loans have first charge security in place over UK property/land to a minimum of 70% loan to value ratio.

Propifi may, at one or several occasions, issue Subsequent Bonds. Subsequent Bonds shall benefit from and be subject to the Finance Documents, and, for the avoidance of doubt, the ISIN, the interest rate, the nominal amount and the final maturity applicable to the Initial Bonds shall apply to Subsequent Bonds. The price of the Subsequent Bonds may be set at a discount or at a premium compared to the Nominal Amount. The maximum total nominal amount of the Bonds (the Initial Bonds and all Subsequent Bonds) may not exceed £25 million unless a consent from the Bondholders is obtained. Each Subsequent Bond shall entitle its holder to and otherwise have the same rights as the Initial Bonds.

Additional risk factors relating to the bonds

Risk of property prices drop

Whether borrowing for buy to let purposes or for a property development, as bridging finance, property mostly secures the loan. In the situation when borrower is not able to repay obligation, loan moves into default, and company can sell the property held as security. There are two crucial things here, how easy the property can be sold and what value it will be sold at. If property prices were to drop, the capital realised from the sale of the property price may be lower than expected. Lending significantly under the value of the property (LTV) should provide sufficient coverage providing the asset was correctly valued at the outset and the market does not drastically drop in value.

Risk of damage to the property

The property is a tangible asset, there is the risk that something may happen to it affecting its value. These risks include natural disasters, fire, robbery or vandalism. If the loan is only secured by a property, the borrower may not have incentive to pay off the debt and the value of the property will not be enough to cover the debt.

Risk of increase interest rates

An important factor of future demand in the BTL market is the path of interest rates. Property have become very attractive asset classes because of relatively cheap financing. Nowadays central banks are preparing to gradually increase interest rates. In the UK, the Bank of England raised rates for the first time in a decade in November 2017, and markets currently expect up to two interest rises for 2018 and further increases in 2019. This means that borrowing costs are expected to rise, which could in turn affect the attractiveness of the housing market.

Liquidity Risk

If the lender is not able to pay back credit, the borrower must sell property on the market, the problems are that we have several property owners and property usually is not liquid, that means it cannot be converted into money quickly. The investors will have to find buyer on their own and all together agree on the price or will have to ask any broker to find buyer, this means additional costs and takes time.

Risk of legal changes

Recent changes in UK to the tax and regulatory treatment of buy-to-let has caused investors to take a step back and assess the viability of these investments. Landlords in higher tax brackets could then end up paying much more tax than they did before, as they'll be paying a percentage of the total rental income rather than the rental income minus their yearly mortgage interest payments. The only tax relief they'll receive is 20% of their interest payment, instead of the entire amount. Since interest costs will no longer be deducted for tax purposes, many private investors will see their tax bill increase substantially. There are also other changes that could take place because of the new rules. A higher tax bracket: the rental income that is used for interest payments must now be declared, which means landlords might find themselves moving up into a higher tax bracket. Negative earnings: some landlords who have smaller profit margins may find themselves in the red after tax – meaning that they could be losing money. Tightening of underwriting standards for BTL mortgages. Potential borrowers may have to undergo stricter affordability testing following a tightening of underwriting rules by the Bank of England's Prudential Regulation Authority (PRA).

Lenders now need to check that the mortgage is affordable either through an interest coverage ratio (ICR) test or through an income affordability test.

Potential adverse legal changes may reduce the number of borrowers, increase competition on the market, negatively affect margins and may affect the repayment of interest from the bonds. It also means a significant difficulty in gaining market share for Propifi.

Risk of Brexit

Over two years after the UK voted to leave the European Union, and still many of the economic and political consequences remain unknown. Investors postponed many transactions, as buyers refuse to strike a deal until there is some sort of certainty over Brexit. Much depends on the final deal between the UK and EU.

One of the effects already observable is drop in net migration from EU citizens to the UK. As immigrants are more likely to live in private rented accommodation, it can be expected that demand for rentals will decrease if this trend continues, especially in bigger cities which absorb most immigrants coming to the UK.

Brexit also had impact on investors, many transactions has been postponed, as buyers refuse to strike a deal until there is some sort of certainty over Brexit.

Dependence on external financing

Propifi is highly dependent on external financing and decrease in demand for its products or reputation damage could significantly reduce access to financing. Usually firms that are the most dependent on external finance have greater likelihood of a falling than firms that are less dependent on external finance.

Rating scale applied by the EuroRating credit rating agency

Rating	Risk description
AAA	Negligible credit risk. Highest level of financial credibility. Rating assigned exclusively where an entity has extremely strong capacity to meet financial commitments.
AA+ AA AA-	Very low credit risk. Very high level of financial credibility. Very strong capacity to meet financial commitments. Low susceptibility to adverse economic conditions.
A+ A A-	Low credit risk. High financial credibility and capacity to meet financial commitments. Average resistance to long-term unfavourable economic financial conditions.
BBB+ BBB BBB-	Moderate credit risk. Good financial credibility and adequate capacity to meet financial commitments in the long term. Increased susceptibility to long-term adverse economic conditions.
BB+ BB BB-	Increased credit risk. Relatively lower financial credibility. Adequate capacity to meet financial commitments under average or favourable economic conditions. High or medium level of debt recovery in the event of default.
B+ B B-	High credit risk. Capability of meeting financial commitments largely conditioned on favourable external conditions. Medium or low level of debt recovery in case of a default.
CCC CC C	Very high credit risk. Very low capability to meet financial commitments even under favourable economic conditions. Low or very low level of debt recovery in case of a default.
D	Extremely high credit risk. Complete lack of capability to meet financial commitments. Without additional external suport the level of debt recovery is very low or close to zero.

Full details on the rating scale applied by the EuroRating credit rating agency are published on the agency's website at: http://www.eurorating.com/en/ratings/rating-scale

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