

Rating Action: Moody's affirms Investcorp's Ba2 rating, outlook negative

Global Credit Research - 31 Oct 2016

London, 31 October 2016 -- Moody's Investors Service has affirmed the Ba2 corporate family rating of Investcorp Bank B.S.C. At the same time, Moody's has affirmed the Ba2 ratings of the backed senior unsecured debt of Investcorp S.A. and Investcorp Capital Limited. The outlook on the ratings remains negative. The rating action follows Investcorp's 25 October 2016 announced acquisition of the debt management business of 3i Group PLC, a global alternative credit manager. The transaction is expected to close in the first half of 2017.

Investcorp's acquisition will be financed through available cash on the balance sheet, which will have a moderately negative impact on the company's solid liquidity profile. In addition, the retained equity portion of CLO deals will add to already substantial co-investment risks on balance sheet. That said, Moody's views the acquisition as potentially having some positive credit implications on Investcorp's business profile, as it will broaden its product and geographical diversification. Over time, distribution synergies are expected as the acquisition will open access to new and incremental sources of capital to both 3i debt management and Investcorp's clients. The acquisition will more than double Investcorp's assets under management to approximately \$23 billion, but given the relatively low fee nature of the business, the contribution to Investcorp's revenue and profit margin is expected to be modest.

RATINGS RATIONALE

Moody's affirmed the Ba2 ratings, reflecting Investcorp's strong franchise in the Gulf Cooperation Council (GCC) region as a leading alternative investment provider to Gulf investors, as well as investors in the US and Europe. Investcorp has a strong reputation and recognizable brand name in the GCC due to its thirty-year-plus track record. The ratings also reflect Investcorp's high financial leverage and balance sheet risk related to its co-investment activities.

Moody's negative outlook on the company reflects the potential that Investcorp might face increasing difficulties in raising new capital or reinvesting clients' capital in the coming year due to the weakening operating environment in the GCC. With a substantial portion of the company's clients located in the GCC region, Moody's considers that Investcorp's assets under management (AUM) growth could slow, which would put pressure on Investcorp's key financial metrics including financial leverage and profitability. While this risk has not yet materialised, with investment cycles being relatively long in alternative investments, Moody's will continue to assess this issue in the coming quarters. Moody's also notes that Investcorp may find it more challenging to stabilise its hedge fund business, which has suffered from net outflows over the last several years, due to the volatile market environment and sustained fee pressure in the fund industry.

WHAT COULD MOVE THE RATINGS UP/DOWN

Upward rating pressure may result from: (i) reduced debt levels; (ii) further reduction in the company's investment portfolio; (iii) growth of Investcorp's clients' AUM, particularly in the hedge fund segment, contributing to substantial EBITDA growth; and (iv) further expansion and diversification of revenue streams, in particular from fund of hedge fund management fees.

Downward rating pressure could result from a weaker financial position driven by: (i) a deterioration in the company's ability to raise new client capital or reinvest client capital that would substantially affect revenue generation capacity; (ii) lower private equity origination and placement activities that would constrain the company's profitability; (iii) material on-balance sheet investment losses; (iv) a reversal in the trend of declining debt and on-balance sheet investment levels; and (v) an erosion in the company's improving capital position.

LIST OF AFFECTED RATINGS

Issuer: Investcorp Bank B.S.C.

..Affirmations:

....Corporate Family Rating, affirmed Ba2 Negative

Issuer: Investcorp Capital Limited

..Affirmations:

...Backed Senior Unsecured Medium-Term Note Program, affirmed (P)Ba2

...Backed Senior Unsecured debt, affirmed Ba2 Negative

Issuer: Investcorp S.A.

..Affirmations:

...Backed Senior Unsecured debt, affirmed Ba2 Negative

..Outlook Actions:

....Outlooks remain Negative

The Probability of Default at Ba2-PD under Investcorp Bank B.S.C. remains unaffected.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Asset Managers: Traditional and Alternative published in December 2015. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Headquartered in Manama, Bahrain, Investcorp Bank B.S. C. (Investcorp) is the principal parent of the Investcorp Group and operates under a wholesale banking license issued by the Central Bank of Bahrain. Investcorp's asset under management were \$10.8 billion as of June 2016.

The last rating action on Investcorp was on 23 March 2016, when Moody's changed the outlook on Investcorp Bank B.S.C. to negative from stable.

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