MOODY'S
INVESTORS SERVICE

CREDIT OPINION
12 January 2021

Update

Rate this Research

RATINGS

Investcorp Holdings B.S.C.

Domicile	Manama, Bahrain
Long Term CRR	Not Assigned
Long Term Issuer Rating	Ba2
Type	LT Corporate Family Ratings
Outlook	Negative

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Dominic Simpson +44.20.7772.1647
VP-Sr Credit Officer
dominic.simpson@moodys.com

Vanessa Robert +33.1.5330.1023
VP-Sr Credit Officer
vanessa.robert@moodys.com

Dimitris Gogos +44.20.7772.1659
Associate Analyst
dimitris.gogos@moodys.com

Investcorp Holdings B.S.C.

Update to credit analysis

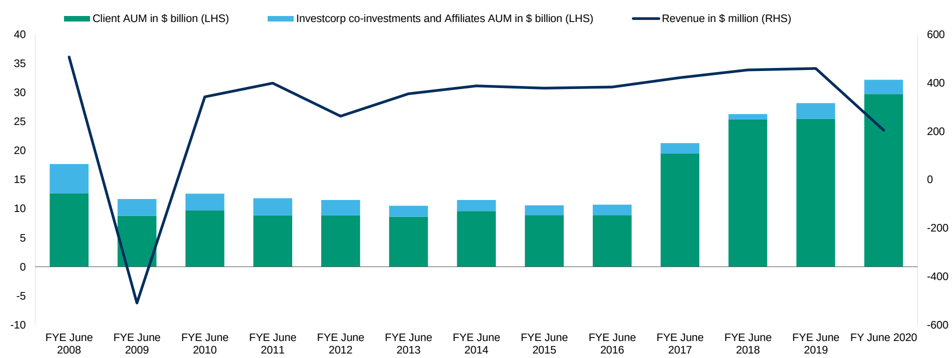
Summary

Investcorp Holdings B.S.C.'s (Investcorp) Ba2 (negative outlook) corporate family rating reflects the company's solid market position in the Gulf Cooperation Council (GCC) region as a leading alternative investment provider, its global franchise, historically healthy operating margins, and good asset retention. Furthermore, Investcorp's level of assets under management and liquidity are expected to remain resilient, and the company has a significant amount of loss-absorbing equity capital notwithstanding the meaningful reduction in FY20. The rating also reflects Investcorp's high leverage, and the impact of the economic downturn prompted by the coronavirus on its financial performance which informs the negative outlook. This impact has already been seen through declines in the level of deal fees and fair value of the company's significant co-investment portfolio which has negatively impacted earnings and leverage metrics.

On 5 June 2020, we affirmed Investcorp's ratings but changed the outlook to negative from stable.

Exhibit 1

The progression of fee income until FY20 had contributed to higher stability of revenue growth



Note: Total AUM for FY2018 was restated as per FY2019, to reflect a change of real estate valorisation to gross value.
Sources: Company reports, Moody's Investors Service

Credit strengths

» Leading alternative asset manager in the GCC region, global reach

» Good AUM resilience rates supported by long-term locked-up capital commitments

» Significant amount of loss-absorbing equity capital and proven capital markets access even in difficult market conditions

Credit challenges

» Earnings headwinds via the economic downturn prompted by the coronavirus

» High financial leverage

» Elevated balance sheet risk owing to large co-investment activities

Rating outlook

The rating outlook is negative reflecting the impact of the economic downturn prompted by the coronavirus on Investcorp's performance.

Factors that could lead to an upgrade

Investcorp is unlikely to be upgraded while the outlook is negative. Factors that could lead to an affirmation of the rating with a stable outlook include the following:

» reduced debt levels with debt/EBITDA remaining consistently below 6x;

» maintenance of good liquidity;

» no increase in level of co-investments in relation to equity;

» continued resilience in level of AUM

Factors that could lead to a downgrade

Factors that could lead to a downgrade include the following:

» Debt/EBITDA sustainably above 6.5x;

» a deterioration in the company's ability to raise new client capital or reinvest client capital that would substantially affect its revenue generation capacity;

» a deterioration in liquidity;

» material on-balance sheet investment losses.

Key Indicators

Exhibit 2
Investcorp Holdings B.S.C.

Key Indicators					
Investcorp Holdings B.S.C. [1]	2020 FY	2019 FY	2018 FY	2017 FY	2016 FY
Assets Under Management (AUM) ($ b)	32	28	26 [4]	21	11
Net Flows ($ mm)	2,357	1,344	1,058	-223	30
Revenues ($ mm) [2]	205	460	454	422	383
AUM Retention Rate (%)	90%	81%	87%	66%	72%
AUM Replacement Rate (%)	196%	131%	144%	92%	101%
EBITDA ($ mm)	93	206	186	160	125
EBITDA Margin (%)	45%	45%	41%	38%	33%
Total Debt ($ mm)	981	1,008	1,135	1,046	1,091
Total Debt/EBITDA (x)	10.6x	4.9x	6.1x	6.5x	8.7x
Total Shareholder's Equity / Self Managed Investments (x)	0.86x	0.98x	0.87x	1.5x	1.2x
Pre-Tax Income ($ mm)	-163	142	138	127	94
Pre-Tax Income Margin (%)	-80%	31%	30%	30%	25%
Stability of Revenue Growth (%) (20 qtr) [3]	-5%	42%	21%	47%	12%

[1] Fiscal year end June 30. [2] Revenue is all operating revenue reported by the company. [3] Stability of revenue growth = the average of quarter over quarter revenue growth rates divided by the standard deviation of revenue growth rates (using the past 20 quarters of growth rates). Here calculated with semi annual information. [4] FY2018 was restated as per FY2019, to reflect a change of real estate valorisation to gross value.
Company reports, Moody's Investors Service

Profile

Investcorp Holdings B.S.C. (Investcorp), previously Investcorp Bank B.S.C., is the principal parent of the Investcorp Group and primarily provides and manages alternative investment products in four main asset classes – private equity, absolute return, real estate and credit management investments – on behalf of institutional clients (71% of total client assets under management (AUM) at FY20) and high-net-worth individuals (private wealth represented 29% of total client AUM). As at end June 2020, Investcorp had total AUM of c.$32 billion.

Investcorp has transitioned to a holding company and renounced its banking license on September 2nd 2019 to better align its operating structure with its business model.

Detailed credit considerations

Global player with strong niche market position in the GCC region

With total and client AUM of $32 billion and $30 billion respectively as at end June 2020 (June 2019: $28 billion and $25 billion) and reported revenue of $178 million as of June 2020 (June 2019: $465 million), the company is a small player in the asset management industry. Its Ba market position reflects its strong brand name in the GCC region, supported by a close to 40-year track record, as well as its global reach especially in North America and Europe. The company benefits from long-standing relationships with leading ultra-high-net-worth and institutional investors in the GCC region. More negatively, at least in the short-term, the company's revenues are being impacted by the economic downturn prompted by the coronavirus.

During FY20, Investcorp's AUM grew by 15% to $32.2 billion, and the company's ability to provide tailored solutions and services to its client base engenders a loyal client base as shown by strong asset retention rates. Furthermore, AUM retention benefits from closed end structures and committed capital.

Since 2017, Investcorp has been actively developing its franchise, incrementally adding AUM, geographic and product diversification, a credit positive – the group has a strategic ambition of reaching $50 billion of AUM over the medium term. In March 2017, Investcorp completed the acquisition of the debt management business of 3i Group plc (Baa1 negative), which contributed an additional $11 billion of AUM. This acquisition more than doubled Investcorp's AUM and contributed $73 million to Investcorp's revenue in fiscal 2019, of which $50 million was fee income. More recent strategic growth initiatives include in 2019, the acquisition of Mercury Capital Advisors, a US investment advisory enterprise, and the acquisition of a majority stake in CM Investment Partners, a US based credit business focused on middle market lending in the United States. Over time, we expect the company to develop cross-selling opportunities within its different divisions.

Investcorp's fund raising capacity remained strong, though reduced, throughout fiscal 2020 with $4.9 billion (FY19: $5.7 billion) in placement and fund raising activity supported by continued client appetite for alternative investments.

Increasing business diversification and global client reach

Investcorp's product and geographic diversification is good and is expected over time to benefit from the implementation of the strategic initiatives. The company's product range is diversified among alternative investments. The company operates under four main segments:

1) Private equity (PE): The segment targets the acquisition of attractive corporate investments in North America, Europe, Asia, the GCC region and Turkey with enterprise values of between $400 million-$800 million. For FY20, private equity AUM (including strategic investments) was stable at $5.8 billion, as new fundraising was largely offset by exits and coronavirus related write-downs.

2) Real estate (RE): The segment targets the acquisition of existing core and core-plus commercial, residential, industrial and logistics real-estate assets (primarily income-earning properties) situated in the 30 largest and most diversified US and European markets (UK and Germany mainly). The majority of real-estate investments are structured in a Shari'ah-compliant manner.

3) Absolute return investments (ARI): The hedge fund business which suffered outflows following the great financial crisis has been restructured through strategic hires, acquisitions, partnerships and fund launches. FY2019 and FY2020 were successful years for the company which raised $1.2 billion and $1 billion respectively of new investor money, and for FY20 AUM increased by 61% to $6.1 billion, due to the strong organic fundraising and also due to the addition of AUM following the joint venture with Tages Group. However, Investcorp's ARI balance sheet exposure is currently less than $100 million.

4) Credit management (CM): Investcorp manages open and closed end funds mainly in collateralized loan obligation (CLO) structures that invest primarily in senior secured corporate debt issued by mid- and large-cap corporates in Western Europe and the US. This business has widened Investcorp's product range and is expected to open up distribution synergies as it will provide access to new and incremental sources of capital to both former 3i Debt Management's and Investcorp's clients. For FY20, credit management AUM increased by 11% to $13.1 billion primarily due to the issuance/pricing of five new CLOs and the acquisition of CM Investment Partners.

Geographic diversification is strong, with client AUM sourced in the GCC region representing 35% of the total as at end June 2020, with almost all the remainder sourced in North America (28%), Europe (25%) and Asia (11%).

Investcorp's distribution profile benefits from good customer granularity. Investcorp has broader client coverage of the GCC region than its peers, with a team of dedicated relationship managers operating through a regional office in Bahrain and through local offices in Saudi Arabia, Qatar and Abu Dhabi. In the US and Europe, Investcorp has a sales team that distributes its products directly to the institutional segment, a segment which the company is increasingly focused on.

Significant financial leverage and co-investment risks are somewhat alleviated by good liquidity and tangible equity

The amount of overall debt factored into our gross debt/EBITDA metric (for Investcorp our standard financial adjustments include the smoothing, via averaging, of asset-based income and activity fees within EBITDA) was relatively stable for FY20 but the level of EBITDA was significantly impacted by the year's result such that the leverage metric increased significantly to a very high 10.6x. Prior to this, Investcorp's leverage had been trending down with gross debt/EBITDA of 4.9x at the end of June 2019 (6.1x end of June 2018) although this is still high compared to Ba-rated peers. We do not expect the significantly reduced EBITDA level at FY20 to be sustained, and with a broad economic recovery underway albeit fragile, we expect a comparably meaningful improvement in the company's results for FY21 and FY22. In turn, we expect the debt/EBITDA metric to reduce to much nearer the levels seen at FY19 and FY18 - one factor that could stabilise the company's negative outlook is debt/EBITDA being consistently below 6x.

Our financial leverage ratio includes the company's short-term debt (following the conversion of the parent from a wholesale bank into a holding company client money has been pooled into a multi-currency revolving loan), although the loan amounts are matched by cash on balance sheet. Excluding this short-term debt, the leverage ratios at FY20 and FY19 reduce to c.8x and 3x respectively.

In addition, through its co-investments, Investcorp makes active use of its balance sheet through principal investments in PE, ARI (including hedge funds), CLO and real estate. The objective is to align its interests with those of its clients and to comply with regulation as far as European CLOs are concerned. For FY20, the disruptive economic impact from the coronavirus significantly affected the company's asset based income which is inherently volatile considering the nature of the co-investments, which are at a slightly higher level than the company's equity. Furthermore, the vast majority of Investcorp's CLO balance sheet exposure is via equity tranches which we believe are more vulnerable than vertical tranches.

A credit strength of Investcorp is its significant amount of loss-absorbing equity capital which counters the company's elevated balance sheet risk. However, total equity reduced meaningfully by 24% (i.e. $277 million) to $868 million for FY20, driven by the net loss, other fair value losses (principally in private equity and credit management), and appropriations. This reduction outweighed the 19% reduction in the level of co-investments to $810 million. Nevertheless, the company continued to meet its target of maintaining co-investments/long-term capital of 1.0x or lower although the metric deteriorated slightly to 0.6x (FY19: 0.5x).

Resilient profit margins have been emerging, but significant loss for FY20 driven by Coronavirus-related impact

Having averaged positive pre-tax income of $135 million with a resilient margin of 30% from FY17-FY19, Investcorp reported a significant pre-tax loss of $163 million for FY20 driven by the impact of the coronavirus on the macro-economic and fiscal environment. Investcorp's asset-based income, via its relatively large amount of proprietary investments, and deal fees were especially impacted. We do not expect the FY20 result to be sustained, and with a broad economic recovery underway albeit fragile, we expect a comparably meaningful improvement in the company's asset-based and overall pre-tax income in FY21 and FY22 with margins returning to a level of around 30%.

The company’s gross revenue can be broken down into three components: (1) AUM fees, (2) deal fees and (3) asset-based income.

AUM fees have been the most stable source of income over the past few fiscal years with a growing contribution to overall revenue which we expect to benefit the quality of Investcorp's future revenue. For FY20, these fees reduced by 6% to $170 million, driven by a 22% decline in private equity fees mainly as a result of the suspension of fees on some investments due to the coronavirus impact. More positively, real estate, credit management and other management fees increased.

In recent years, Investcorp's revenue base has been very reliant on deal fees which are less predictable than AUM fees and represented around 50% of the company's fee revenue for FY19. These fees depend on the acquisition and placement of new investments, the sale and exit of investments (realizations) and the performance of existing investments. The main driver of the reduction in the company's fee income for FY20 was a 29% fall in activity fees to $119 million reflecting the impact of the coronavirus which resulted in reduced levels of acquisitions, placements and exit activity in the last part of the financial year. Performance fees, also impacted by the coronavirus, reduced by $29 million to a loss of $1 million.

The largest contributor to Investcorp's FY20 result was the $110 million asset-based loss. Asset-based income which historically has contributed meaningfully to Investcorp's revenue base, is the most volatile profitability component as it is based on the annual return on the company's proprietary investments which are principally in private equity and CLOs. Due to the impact of the coronavirus, which resulted in a full writedown of three retail sector investments, private equity returned a loss of $96 million. Credit management (which includes the CLO investments) and strategic investments also returned losses of $22 million and $27 million respectively in contrast to a real estate profit of $31 million.

Longer term, we expect Investcorp's strategic acquisitions and growth initiatives in all divisions including the ARI business in the US, and the PE business in Asia, to deliver cross-selling opportunities, that should support revenue growth.

Liquidity analysis

Investcorp’s credit profile benefits from its good liquidity management practices and good liquidity position. Total accessible liquidity at the end of June 2020 was $993 million (excluding a $233 million balance available from the multi-currency term and revolving loan) albeit reduced from $1.1 billion as of the end of June 2019 principally driven by operating activity. Total accessible liquidity on the same basis increased to $1,035 million at the end of September 2020. This liquidity position covers all of Investcorp's outstanding debt maturing over the next five years.

Environmental, Social and Governance (ESG) Considerations

Environmental

Macro/Sector: The asset manager sector is classified as "low" risk in our Environmental Heatmap. Sectors in the low risk category have either no sector-wide exposure to meaningful environmental risks or, if they do, the consequences are not likely to be material to credit quality or ratings. Typically, this would mean that according to our most likely scenario, existing and prospective environmental risks have minimal potential to move ratings over the next seven years.

Asset managers' own environmental footprints do not typically raise credit concerns. Environmental risks to asset managers are largely indirect, through their investment exposures and decision making. This indirect exposure is less significant for asset managers that are well diversified both by industry and geography. However, environmental risks are more significant for asset managers with concentrated geographical exposures to climate risks, or investments in fossil-fuel infrastructure and energy transportation.

Issuer: Investcorp's exposure to environmental risks is moderate, consistent with our general assessment for the asset manager sector.

Social

Macro/Sector: Asset managers generally have moderate exposure to social risks because they are reliant on human-capital assets. Social risks may stem from internal organizational dynamics, external customer relations, and demographic factors. The industry is absorbing information technology that is giving rise to risks from changes in management systems and personnel relations, as well as from interactions with intermediaries and clients. Asset managers are increasingly exposed to the risk of breaches of data security and customer privacy, which can affect their reputations and client retention. Additional risks in some regions stem from new disclosure requirements of organizational diversity, gender pay, and board composition. The risk of population ageing may constrain asset growth in affected countries. Asset managers who adopt socially ESG-driven agendas may better appeal to investor populations who show increasing concern for these issues.

Issuer: Investcorp's exposure to social risks is consistent with our general assessment for the asset manager sector.

Governance

Like all other corporate credits, the credit quality of Investcorp is influenced by a wide range of governance-related issues, relating to financial, managerial, ownership or other factors, all of which can be exacerbated by regulatory oversight and intervention.

While Investcorp's investments in illiquid asset classes entail above average risk levels, the group has strong risk management processes that mitigate various governance risks. It also displays high levels of transparency. Under the oversight of its Board of Directors, the Group's management team has a strong track record and experience.

Rating methodology and scorecard factors

Exhibit 3

Investcorp Holdings B.S.C.

Investcorp Holdings B.S.C.									
Rating Factors									
Asset Managers Scorecard (weights)[1]	Aaa	Aa	A	Baa	Ba	B	Caa	**Score**	**Adjusted Score**
Business Profile								**Baa**	**Ba**
Factor 1: Market Position (25%)								**Baa**	**Ba**
Scale and Franchise Strength					X				
AUM Resilience		X							
Factor 2: Business Diversification (25%)								**Baa**	**Baa**
Geographic and Product Diversification			X						
Distribution					X				
Financial Profile								**B**	**Ba**
Factor 3: Financial Flexibility (30%)								**Caa**	**B**
Debt / Adjusted EBITDA							10.6x		
Total Shareholder's Equity / Self-managed Investments							0.9x		
Factor 4: Profitability & Revenue Stability (20%)								**Ba**	**Baa**
Pre Tax Income Margin (5 yr ave)						7.2%			
Stability of Revenue Growth (20 qtr, YoY)					-4.8%				
Operating Environment								**Baa**	**Baa**
Stand-alone Credit Profile Before Qualitative Notching Factors								**Ba2**	**Ba2**
Indicated Instrument-level Outcome									**Ba2**

[1] The scorecard in this rating methodology is a relatively simple tool focused on indicators for relative credit strength. As described in the methodology, there are various reasons why scorecard-indicated outcomes may not map closely to actual ratings.

Moody's Investors Service

Ratings

Exhibit 4

Category	Moody's Rating
INVESTCORP HOLDINGS B.S.C.	
Outlook	Negative
Corporate Family Rating	Ba2
INVESTCORP CAPITAL LIMITED	
Outlook	Negative
Bkd Senior Unsecured	Ba2

Source: Moody's Investors Service

REPORT NUMBER 1257685

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

MOODY'S INVESTORS SERVICE