



Fitch Affirms Alcentra's IMQR at 'Excellent'

Fitch Ratings-London-10 August 2018: Fitch Ratings has affirmed Alcentra Ltd's (Alcentra) Investment Management Quality Rating (IMQR) at 'Excellent' with a Stable Outlook.

KEY RATING DRIVERS

The affirmation of Alcentra's IMQR reflects the broad stability in processes, staffing and corporate structure. The rating is driven overall by Alcentra's well-defined and robust investment processes, the depth and calibre of investment staff and the high quality support provided by Alcentra's institutional owner. The company has grown and diversified (across both product, strategy and investor dimensions) while commensurately growing human and technology resources. Fitch expects the risk-management framework to benefit from a project that is underway to align Alcentra's policies and procedures with those of other boutiques in the Bank of New York Mellon Corporation (AA-/Stable/F1+).

Alcentra's rating is based on the following category scores:

Investment Process: Excellent
Investment Resources: Excellent
Risk Management: Strong
Investment Performance: Consistent
Company and Client Servicing: Excellent

Investment Process

Fitch considers Alcentra's investment process to be 'Excellent', underpinned by a robust fundamental bottom-up and top-down research framework. All credits are subject to a preliminary credit screening followed by more detailed due diligence. In 2017, Alcentra integrated Environmental, Social and Governance indicators to its analysis process. Credit monitoring is continuing, formalised in regular investment committee meetings and portfolio reviews.

Investment Resources

The number and experience of Alcentra's investment professionals supports Fitch's view that Investment Resources are 'Excellent'. Alcentra had 38 investment professionals in Europe as of end-2017, responsible for a total of 46 funds and mandates. Alcentra added net 24 staff globally in 2017, notably in support of its

direct lending activities and including several senior appointments: Alcentra has moved from a co-chief investment officer structure to a single global chief investment officer, and added an operational risk director. Alcentra has strong relationships with its administrators, custodians and trustees. It also benefits from the oversight, experience and resources, such as IT, legal and human resources, of its institutional owner.

Risk Management

Fitch considers Alcentra's Risk Management to be 'Strong'. The risk framework is robust, providing suitable coverage of the main risks and effective, independent risk oversight and controls. There are comprehensive policies and procedures in place to ensure compliance with regulatory rules. In 2017, Alcentra hired a senior director to review its risk and compliance framework both in terms of ensuring best practice and aligning policies and procedures with other investment boutiques owned by the BNY Mellon Group. Fitch expects this process to strengthen the risk control environment further.

Investment Performance

Alcentra manages a range of investment products with differing characteristics. The open-ended funds have performed well. The largest of these funds within the rating scope (a loan fund) has generated strong performance over a prolonged period of time both in nominal and risk-adjusted terms. Furthermore, this fund has demonstrated strong downside protection in stressed market conditions.

All debt tranches of Alcentra's pre-crisis CLOs paid in full demonstrating good performance for debt-holders and all post-crisis CLOs are performing with equity returns above peer medians in almost all cases. The direct lending strategies are more recent, but Alcentra's middle-market experience is significantly longer (dating back to 1998). Public information on comparable funds and strategies is limited, but Fitch believes the returns generated by the direct lending funds are in-line with market averages such as private debt metrics published by Preqin.

Taking into consideration both the demonstrably strong performance of the open-ended funds, the consistent performance of the CLOs and the more recent performance history of the direct lending funds, and their respective asset weights, Fitch considers Alcentra's overall investment performance consistent with its stated investment objectives and investor expectations. Sustained strong performance of the open-end funds, in combination with a longer-track record to assess for the direct lending funds could lead Fitch to revise the Investment Performance score to 'Strong'.

Company and Client Servicing

Alcentra's Company and Client Servicing score of 'Excellent' is driven by its strong

franchise as one of the largest and longest-established European sub-investment-grade credit asset manager, and its strong and sustained profitability. Having the BNY Mellon Group as its institutional owner is a highly positive factor in Fitch's analysis. Client servicing and reporting is very sophisticated, reflecting Alcentra's institutional investor base.

Profile

Alcentra is a diversified sub-investment-grade credit manager with expertise in structured credit, secured loans, direct lending, mezzanine loans, high-yield bonds, special situations and multi-strategy. Alcentra Group had assets under management of USD35.7 billion as of December-2017 globally, split evenly between the US and Europe, with 145 employees globally, 66 of whom are investment professionals.

RATING SENSITIVITIES

The rating may be sensitive to material changes in one or several of the five IMQR pillars. A material adverse deviation from Fitch's guidelines for any key rating drivers could result in a downgrade. This could be structural deterioration in investment performance, excessive risk-taking, the departure of key investment staff or deterioration of the company's financial health.

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Applicable Criteria

Investment Management Quality Ratings (Assessing Active, Passive & Alternative Investment Managers, Strategies & Funds) (pub. 06 Mar 2017)
(<https://www.fitchratings.com/site/re/893989>)

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