ARC Ratings, S.A. accords ratings to Aqueduct European CLO 5-2019 DAC Structures

ORIGINATOR	ISSUE RATING	
	1ST STRUCTURE	
Aqueduct European CLO 5-2019 DAC	AA(sf)	Senior Funding Facility (AA(sf), with stable outlook)
	2ND STRUCTURE	
	AAA(sf)	Senior Funding Facility (AAA(sf), with stable outlook)
	AA(sf)	Mezzanine Funding Facility (AA(sf), with stable outlook)
RATING DATE	**NEXT REVIEW DATE**	
24 June 2019	24 June 2020	

ARC Ratings, S.A. (ARC) has accorded final, long-term public ratings to Aqueduct European CLO 5-2019 Designated Activity Company Structures. With regards to the 1st structure, ARC has accorded a final, long-term public rating of 'AA(sf)' to the Senior Funding Facility, with a stable outlook. With regards to the 2nd structure, ARC has accorded a final, long-term public rating of 'AAA(sf)' to the Senior Funding Facility and 'AA(sf)' to the Mezzanine Funding Facility, both with stable outlooks.

COMPANY PROFILE

Aqueduct European CLO 5-2019 Designated Activity Company (the 'Borrower') is a private company with limited liability incorporated under the laws of Ireland. As identified in the Warehouse Deed, the Borrower expects to acquire and warehouse a portfolio of the collateral obligations prior to the CLO closing date.

The rating addresses the legal and financial structures of the two transactions, the quality of the underlying collateral, the management capability of the Collateral Manager, the timely interest and ultimate repayment of principal.

TRANSACTION OVERVIEW & CAPITAL STRUCTURE

ARC was provided with two possible transaction structures:

- BNPP's Senior Funding Facility (attachment point at 15% and detachment point at 100%) and Subordinated VFNs.
- BNPP's Senior Funding Facility (attachment point at 40% and detachment point at 100%), Mezzanine Funding Facility (attachment point at 20% and detachment point at 40%) and Subordinated VFNs.

RATING RATIONALE

Key rating drivers include:

- Credit Enhancement:

With regards to the 1st transaction structure, ARC believes the credit enhancement provided is sufficient to protect the Senior Funding Facility at a 'AA(sf)' rating level (given attachment point at 15%) against losses from the portfolio – since this amount of losses will be first absorbed by the Subordinated VFN Holders, ARC tested the sufficiency of the credit enhancement available, given the factors detailed below.

In the 2nd scenario, the credit enhancement is sufficient to absorb the losses at a 'AAA(sf)' rating level for the Senior Funding Facility (given attachment point at 40%) as these amounts of losses will be first absorbed by Mezzanine and Subordinated VFNs Holders; and at a 'AA(sf)' rating level for the Mezzanine Funding Facility (given attachment point at 20%) as this amount of losses will be first absorbed by the Subordinated VFN Holders considering the following factors:

- 'B/B-'Weighted Average Asset Quality: The weighted average credit rating of the indicative portfolio is 'B/B-'. Whilst issuers rated in the 'B/B-' rating category denote relatively weak credit quality, ARC considers the notes are unlikely to be affected by the projected level of defaults (weighted average 1-year probability of default rate is 7.96%) - particularly given the level of credit enhancement present.
- Recovery Expectations: The indicative portfolio consists of 89.7% Senior Secured Obligations.

With regards to the 1st structure, ARC stressed the recoveries of the portfolio by assuming a higher concentration of assets with weak recovery prospects, ultimately resulting in a 37.3% recovery rate assumption in ARC's 'AA(sf)' scenario.

In terms of the 2nd structure, the recovery rate assumption resulted in a 31.9% in ARC's 'AAA(sf)' scenario and 37.3% in ARC's 'AA(sf)' scenario. The recovery rate for the Senior Funding Facility is lower in the second proposed structure due to the higher expected loss rates modelled for the 'AAA(sf)' rating level.

These are conservative recovery assumptions for a 'AA(sf)' and 'AAA(sf)' rating levels.

- Collateral Manager Expertise: HPS Investment Partners CLO (UK) LLP offers investment management services. The firm was incorporated in 2016 and focuses on non-investment grade credit.
- Industry and Regional Diversification: The portfolio assets exhibits broad industry distribution with the largest sectors being Healthcare (19.6%) and Business Services (18.6%). Regional distribution is primarily concentrated in four countries; France, the United Kingdom, Germany and the United States. However, the economic strength of the respective nations, the otherwise diversified nature of the portfolio and the fact that a number of the issuers are multinationals assists in balancing this exposure. The largest obligor of the portfolio represents not more than 2.1% of the Portfolio Notional Amount and the five largest obligors represent 10.1%.

SUMMARY OF RATING METHODOLOGIES

ARC has applied its Global Structured Finance Rating Criteria (updated in September 2018) in conjunction with its Collateralised Loan Obligation (CLO) Rating Criteria (updated in February 2019). These methodologies are freely available from www.arcratings.com.

THIS DISCLOSURE IS FOR INFORMATION PURPOSES ONLY

ARC Ratings, S.A.

11 Hollingworth Court

Turkey Mill, Ashford Road

Maidstone, Kent ME14 5PP

UNITED KINGDOM

Phone: +44 (0)1622 397350

E-mail: arcratings@arcratings.com

Website: www.arcratings.com

Key Contacts:

Paulina Mileryte
Lead Analyst
paulina.mileryte@arcratings.com

Sophie Crofts
Back-up Analyst
sophie.crofts@arcratings.com

Emma-Jane Fulcher
CRO & Panel Chairperson
emma.fulcher@arcratings.com

Note that ARC is not a legal, tax or financial adviser, and only provides a credit opinion of the rated securities. For example, a rating does not cover a potential change in laws nor can it be regarded as an audit. Moreover, ARC is not a party to the transaction documents. Users of our credit ratings should familiarise themselves with the transaction documents / mechanics and should form their own views in this respect. They should not rely on ARC for legal, tax or financial advice, and are encouraged to contact the relevant advisers.

ARC Ratings, S.A. is registered as a Credit Rating Agency (CRA) by the European Securities and Markets Authority (ESMA), within the scope of the REGULATION (EC) N° 1060/2009 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL, of 16 September, and recognised as External Credit Assessment Institution (ECAI).

Ratings assigned by ARC Ratings represent opinions on the capacity and willingness of an entity to make all required payments on a given obligation in a timely manner.

The rating(s) assigned by ARC Ratings in this report was / were sought by the entity whose financial commitments are being rated.

Prior to the assignment or revision of a rating ARC Ratings provides to the entity whose financial commitments are being rated the documents that substantiate the rating to be attributed. This entity is thus given the opportunity to clarify or correct factual details, thus allowing the rating assigned to be as accurate as possible. The comments made by the entity whose financial commitments are being rated are taken into account by ARC Ratings in the assignment of the rating.

ARC Ratings, S.A. historical default rates are published in the European Securities and Markets Authority Central Repository (CEREP) which can be accessed on the website cerep.esma.europa.eu/cerep-web/. ARC Ratings default rate is the probability of lack of full and timely payment of capital or interest or of the occurrence of any event that explicitly indicates that the future full and timely payment of those commitments will not occur (e.g., in case of insolvency).

Ratings do not constitute a recommendation to buy or sell, but only one of the factors to be weighted by investors.

Throughout the entire period during which ratings are valid, ARC Ratings monitors the issuer's performance on a constant basis, and may even bring forward the date of the review unless stated as point in time. Hence, prior to an investor using a rating, ARC Ratings recommends that it be confirmed, namely by consulting the list of public ratings available on the website www.arcratings.com.

ARC Ratings' ratings are assigned based on information, which may include confidential information, collected from a wide group of sources, which may include the entity whose financial commitments are subject to rating. ARC Ratings uses and treats this information with due care and attention. Although all due care was taken in the collection, cross-checking and processing of the information for the purposes of the rating analysis, ARC Ratings cannot be held liable for its accuracy. ARC Ratings must make sure that the information has a minimum level of quality prior to assigning a rating based on such information.

In the rating process, ARC Ratings adopts procedures and methodologies aimed at ensuring transparency, credibility and independence, and also that rating classifications are not influenced by situations of conflict of interests. Any exceptions to these principles are disclosed by ARC Ratings together with the rating of the financial commitment in question.