ARC Ratings S.A. affirms the public, final long-term 'BBB(sf)' rating accorded to the EUR 200m Notes issued by BUMA LUX II Europe S.C.S. SICAV-RAIF, with stable outlook

London, 16 September 2020 - ARC Ratings S.A. (ARC) has affirmed the final, long-term 'BBB(sf)' rating to the EUR 200m Notes issued in bearer form by BUMA LUX II Europe S.C.S. SICAV-RAIF, with stable outlook.

The Notes have an aggregate nominal amount of up to EUR 200m and an extended Maturity Date of 22 November 2033. The Issuer shall use all proceeds received from the issuance of the Notes in accordance with its corporate purpose as well as its investment policy to acquire participations in one or more target funds which, in turn, and in addition to investing in liquid assets and derivatives for hedging purposes, invest into debt instruments in the form of debt securities such as bonds, promissory notes and loans.

This Press Release should be read in conjunction with the accompanying rating report, published on 16 September 2020, available at www.arcratings.com.

ISSUER	CLASS / TRANCHE	TRANCHE AMOUNT	RATING CLASS	RATING	OUTLOOK	NEXT REVIEW DATE
BUMA LUX II Europe S.C.S. SICAV-RAIF	Notes issued in bearer form	EUR 200m	CLO	BBB(sf)	Stable	16 September 2021

TRANSACTION OVERVIEW

BUMA LUX II Europe S.C.S. SICAV-RAIF ('Fund') is an umbrella fund, the investment objective of the Fund is to provide investors with periodic returns from an actively managed portfolio of predominantly European Debt Obligations which are primarily Senior Secured Obligations. The Fund raises debt capital by issuing limited partnership shares and Notes. The structure of the transaction has remained unchanged since ARC accorded the rating in September 2019, in that there is still only one sub-fund underpinning the Notes issued – BUMA LUX II ECM which is actively managed by Wells Fargo Asset Management ('WFAM', 'Asset Manager').

The Current Asset Portfolio Amount is EUR 182.15m as at 31 July 2020, with a Maximum Portfolio Amount of EUR 285.7m. The portfolio predominately contains Leveraged loans (78.4%), High Yield Bonds (20.3%) and a small proportion of Corporate Bonds (1.3%). Portfolio obligors operate across a broad spectrum of industry classifications with the highest concentrations in Computer & Electronics, and Business services, with 17% and 15% respectively of the Total Portfolio Amount. From a currency risk perspective, the portfolio is primarily exposed to Euro denominated assets, making up 89.1% of the portfolio, with the remainder in GBP (7.9%) and USD (1.6%) assets.

Pertinently, WFAM has recently updated their equity investment limit, reducing the maximum proportion of equity like instruments allowed in the Sub-fund to 5% of NAV, from 15% of NAV. ARC expects the Sub-fund's equity exposure in relation to the NAV to remain low (c. 1-1.5%); this view has been formed by the information provided by WFAM in addition to the 0% historical and current equity exposure percentage. As such, should there be a prominent or sudden rise in the Sub-fund's equity exposure, above ARC's expectations and beyond the 5% investment limit, which in turn causes a significant deterioration in the credit quality of the portfolio, rating action could follow.

RATING RATIONALE

Key Rating Drivers:

- **Covid-19:** The outbreak of Covid-19 caused European economies to contract in 2020 and led to unprecedented pressure in the European High Yield Bond and Leverage Loan markets as a consequence of the government-imposed enforcement measures. Subsequently, there was a wave of downgrades from the rating agencies reflecting the ongoing credit concerns. More recently, however, the European economies and more specifically the leveraged finance market have begun displaying signs of recovery, as issuance volumes have started to increase above levels seen in the first quarter of 2020.

- To account for the negative impact of Covid-19 and the potential for there to be a second wave of downgrades in the leveraged finance market, ARC has applied a combination of stresses after examining each industry and country comprising the Sub-fund's portfolio. In line with what was seen in the market, higher stresses have been applied to industries and countries which suffered a greater impact from Covid-19. Although this resulted in an increase in the portfolio's loss rate, ARC notes that the structural enhancements in place are sufficient to protect the transaction against expected losses at 'BBB(sf)' rating level.
- **Portfolio Credit Quality:** The weighted average asset credit rating of the Sub-fund is 'B/B-', these reflective of ARC's conservative rating assumptions where more than one rating is available. Despite the weighted average rating of the Sub-fund deteriorating slightly, there has only been one company 'Lecta' which has defaulted (0.53% of the current portfolio balance) in the last year. This company had already defaulted prior to the crisis in December 2019 and subsequently defaulted again in May 2020 due to Covid-19 pressures. This shows a degree of resilience by the assets in the portfolio, particularly as the sharp contraction in economic activity has created financial difficulties and defaults for high-yield issuers, some of whom are not overly leveraged. This is evidenced by European high-yield bond default rates increasing to 2.4% in the first-half of 2020 from 1.2% at the end of 2019. Thus, ARC is of the opinion that credit risk in the portfolio is already incorporated into the NAV, given current yield levels already have already priced in the risk. Given the evolving macro-economic environment resulting from Covid-19, ARC will continue to monitor the ratings of the assets within the portfolio closely.

- **Industry diversification:** The portfolio of assets exhibits broad industry distribution with the largest sector being Computer and Electronics (17.39% of the Total Asset Value). Assets comprising this sector are predominantly in the software and IT services sub-sectors, ARC is of the opinion that this is a credit positive given the defensive nature of the sectors. An example of such would be Avaloq Group (rated 'B' by two other leading credit rating agencies) which is a software company specialising in banking software and the largest contributor to the Sub-fund's performance. The potential long-term impacts on these sub-sectors are predicted to be positive, in ARC's opinion, due to the switch to remote working and online learning. Forecasts for IT spending indicate continued demand for cloud infrastructure services whilst specialised software, communications equipment and telecom services are anticipated to experience increased demand.

- **Regional distribution:** The portfolio is primarily concentrated in the United Kingdom (23.03% of the Total Asset Value), Germany (13.83% of the Total Asset Value) and Luxembourg (13.45% of the Total Asset Value). Whilst exposure to the United Kingdom is high, WFAM highlighted that this was often due to companies being domiciled in the United Kingdom, but not actually trading there. This is supported by the currency exposure where only 7.86% of the portfolio is exposed to GBP, whilst 89.08% is exposed to EUR. The portfolio is predominantly exposed to economically strong European countries with only 3.13% of the Total Portfolio Amount comprised of assets from weaker sovereigns that have been more severely affected by Covid-19.
- **Credit Enhancement:** The structural enhancement mechanisms in place for the Notes, include a minimum equity buffer of 30% which, combined with excess spread, is sufficient to protect the Notes at a 'BBB(sf)' rating level in ARC's worst-case scenario. In this scenario, ARC modelled the Sub-funds equity exposure reaching the maximum amount permissable, in this regard WFAM has reduced its internal investment limit to 5% of NAV from 15% of NAV.
- **ARC Cashflow Model:** ARC ran its cash flow model to assess the ability of the transactional cash flows to repay interest on a timely basis and principal on an ultimate basis by the Maturity Date. ARC's cashflow analysis assumed that the assets with the highest margins defaulted first, up to the level determined in ARC's default model. ARC also ran front and back loaded vectors and calculated that the transaction with its current level of credit enhancement is able to withstand stresses commensurate with a 'BBB(sf)' rating scenario.

RELATED CRITERIA AND RESEARCH

ARC Ratings' Global Structured Finance Rating Criteria (updated September 2019)

ARC Ratings' Global Collateralised Loan Obligation (CLO) Rating Criteria (updated February 2020)

ARC Ratings' Global Master Criteria for Rating Funds and Asset Managers (updated November 2019)

BUMA LUX II Europe S.C.S. SICAV-RAIF – Universal Investment Luxembourg S.A. Report September 2020

THIS DISCLOSURE IS FOR INFORMATION PURPOSES ONLY AND SHOULD BE READ IN CONJUNCTION WITH THE RESPECTIVE RATING REPORT

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

Site: www.arcratings.com

Key Contacts:

Sophie Crofts	Garth Campbell	Mark Vrdoljak	Philip Walsh
Senior Structured Finance Analyst	Structured Finance Analyst	Head of Structured Finance	Chief Rating Officer
Lead Analyst	Back-up Analyst		Panel Chairperson
sophie.crofts@arcratings.com	garth.campbell@arcratings.com	mark.vrdoljak@arcratings.com	philip.walsh@arcratings.com

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This Review Report should be read together with initial Rating Report and with the subsequent Review reports.

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