Appendix to Criteria for Rating Financial Services Companies: Asset Management Issuer Credit Ratings

Contents

Introduction

1. This criteria appendix acts as a supplement to GCR's Criteria for Rating Financial Services Companies, published in May 2019, and consequently must be read in conjunction with the criteria, which can be found at GCRratings.com/criteria.

Scope of the Criteria

2. GCR accords two types of ratings for Asset Managers, 'issue(r) credit ratings' and 'management quality ratings'. The below criteria explicitly describes how GCR formulates the issue(r) credit ratings for an Asset / Wealth Manager. To view the 'management quality' rating criteria, please see the criteria titled 'Global Master Criteria for Rating Funds and Asset Managers', published March 2017. GCR also includes under the scope of this criteria more general 'Wealth Managers', whom may not take Assets under management but provide advice or brokerage services.

3. GCR will apply the Asset Management criteria (below), when the rated entity derives a majority of revenues from the management (including management fees, brokerage fees and investment performance) of third-party funds or private retail wealth.

Component 1: Operating Environment

Country Risk Score

4. GCR assess the country risk score of an Asset Manager by weighing the Asset Under Management ("AUM") or brokerage revenues of the client base. This is processed in line with the country risk section within the Criteria for the GCR Ratings Framework.

Sector Risk Score:

5. GCR will use the financial institutions risk score for the country of the Asset Managers domiciliation, as a starting point and then make up to three negative adjustments to create the sector risk score for asset managers. GCR can make negative adjustments if any of the following exist:

6. There is less prudential regulatory oversight for an Asset / Wealth Manager than a commercial bank operating in the same country,

    - The manager is exposed to higher market conduct scrutiny or potentially sensitive to regulatory or legislative changes,
    - Access to market funding is typically weaker,
    - Industry profit margins are weaker for Asset/ Wealth Managers than commercial banks,
    - Replacement risk is very high or barriers to entry are lower than commercial banking.

7. Conversely, there may be a counteracting positive adjustment if the industry of the entity is prudentially regulated or has a protected or critical market infrastructure role or if the bank sector starting point is already very low.

Component 2: Business Profile

Component 2, Factor A: Competitive Position

8. GCR have made changes to the underlying subfactors that guide the competitive position score for an Asset/ Wealth Manager versus a Financial Services Company. These include:

- Competitive Advantage: When assessing the competitive advantage of an Asset Manager, GCR looks at the scale (including measuring assets under management (AUM)), market position, track-record and brand strength of the company versus global, regional or national peers.

- Diversification: GCR looks at the diversification of revenues and AUM by asset class, distribution channel, geography, investors (typically a diversified retail investor base is seen more positively than an institutional investor base) and products.

Table 1: Competitive position

Assessment	Score	Description*
Highest	4 to 5	A globally diverse Asset Manager, with AUM of over $500bln, strong brand and long track-record. AUM is well-diversified by asset class, distribution and investor base, and geography.
High	2 to 3	A top tier regional Asset Manager, with AUM of over $250bln, well-established brand and track-record. AUM is diversified by asset class. There is a material amount of geographic diversification, a broad range of investors and no clear product or asset class concentrations.
Intermediate	-1 to 1	A top tier national asset manager, or a second-tier asset manager with substantial AUM, operating materially across more than one country. Typically, will have a strong national brand and a long track-record. Relative to its core markets, there is good diversification of AUM by asset class and investor base.
Low	-4 to -2	A second or third tier national asset manager, typically with no material geographic diversification. Developing brand and/ or track-record versus local peers. GCR would expect some diversification of the AUM by asset class, investor base or products.
Lowest	-10 to -5	A lower tier asset manager, with a limited track-record or brand. There may be significant asset class, distribution or investor base concentrations.

*The above boxes highlight typical characteristics of the high, intermediate and low (and so on) assessments, and are utilised in conjunction with the operating environment anchor, and relative to the markets of the issuer's operations. It is likely that an entity has one or more characteristic across different boxes. GCR allows analytical decision making to decide what the most pertinent factors for each rated entity are. However, to achieve a stronger score the entity is likely to relfect a number of cumulative strengths. Conversely, any one risk can bring the score down to a much weaker level.

9. GCR may also make an adjustment to the initial competitive position score for any of the following factors:

a) Investment Performance & AUM Growth: The success of an asset manager can best be assessed on the stability of its investment performance against major indices or benchmarks and the growth of its assets under management ('AUM'). If the company is outperforming / underperforming the market or growing / shrinking AUM quicker than the market, GCR can make a positive/ negative adjustment to the initial score.

b) Distribution networks: GCR view positively controlled distribution networks, with low fees and commissions paid to brokers. Conversely, limited control over distribution or price sensitive brokerage activity is viewed more negatively.

c) Protected government role: If the Asset Manager has a protected role by one or more government, which leads to more stable AUM than the market average, GCR could raise the risk score.

d) ESG: GCR may also make any adjustments seen for Environmental or Social risks facing the entity. GCR will make adjustments for these factors, on a case by case basis.

Component 2, Factor B: Management & Governance

10. Full adoption of the criteria from the GCR Ratings framework.

Component 3: Financial Profile

Component 3, Factor A: Leverage & Cash Flow

11. When assessing the initial cash flow leverage of an Asset / Wealth Manager, GCR use the same approach, including all ratios and adjustments stated in the main Financial Services Companies ("FSC") criteria.

12. However, typically, GCR will cap the cash flow and leverage assessment within the high category (+2 to +3) if the asset or wealth manager doesn't have a strong and diversified competitive position and investment track-record, or if it has a limited track-record in raising and managing debt.

13. GCR can also make an adjustment if the Asset/ Wealth Manager takes on a significant amount of on-balance sheet investment risk. In this case, cash flow wouldn't provide a full picture of the risk. As a result, GCR may choose to use an adjusted leverage ratio from the non-bank financial institutions criteria (see page 24 of the Criteria for Rating Financial Institutions).

Component 3, Factor B: Earnings versus Risk

14. When assessing the earnings versus risk score for an Asset/ Wealth Manager, GCR firstly takes into account the level of profitability, on a margin basis, in line with the FSC criteria.

15. However, GCR will routinely make haircuts to the earnings before interest, tax, depreciation and amortisation ('EBITDA') line for revenues that GCR consider to be less stable. Broadly, GCR will include 100% of management fees, 75% of investment performance fees, 75% of realized of balance sheet driven investment income and 35% of unrealized balance sheet driven income. All other income will be assessed on a case by case basis, measured on their long-term stability.

16. Furthermore, GCR may make an adjustment to the initial score if the balance sheet risk exposes the Asset Manager to any of the risks detailed in paragraph 28 of the FSC criteria or generally higher amounts or unrealized/ realized valuation gains. GCR may also choose to make a negative adjustment if the investment risk exposes the manager to interest rate, currency, commodity, equity or any other market-based movements.

17. GCR may also make negative adjustments if the asset manager has a high fixed cost base or runs inefficient operations.

Component 3, Factor C: Liquidity

18. GCR will analyse balance sheet liquidity for Asset Managers broadly in line with FSC criteria or FI Criteria, depending on nature of the company. However, we will also analyse the liquidity of the invested assets to ensure that the Asset Manager can adequately cope with AUM outflows from investor concentrations, country or market-led stress events, seasonal demands and other potential liquidity events, especially if the AUM have a defined term of repayment.

19. Typically, GCR will cap (i.e. no higher than) Asset/ Wealth Managers at the intermediate range (-1, 0, +1) as GCR believes such entities should maintain inherently higher balance sheet and invested asset liquidity than other FSCs, given their potentially confidence/ market sensitive nature of future cash flows.

Component 4: Comparative Profile

20. All elements are the same as the FSC criteria

Final Rating Adjustment Factors

21. Broadly in line with the FSC criteria, although if structural subordination exists due to regulatory oversight, GCR may reflect this risk in line with the Criteria for Rating Financial Institutions.