

Arrow Global Group PLC

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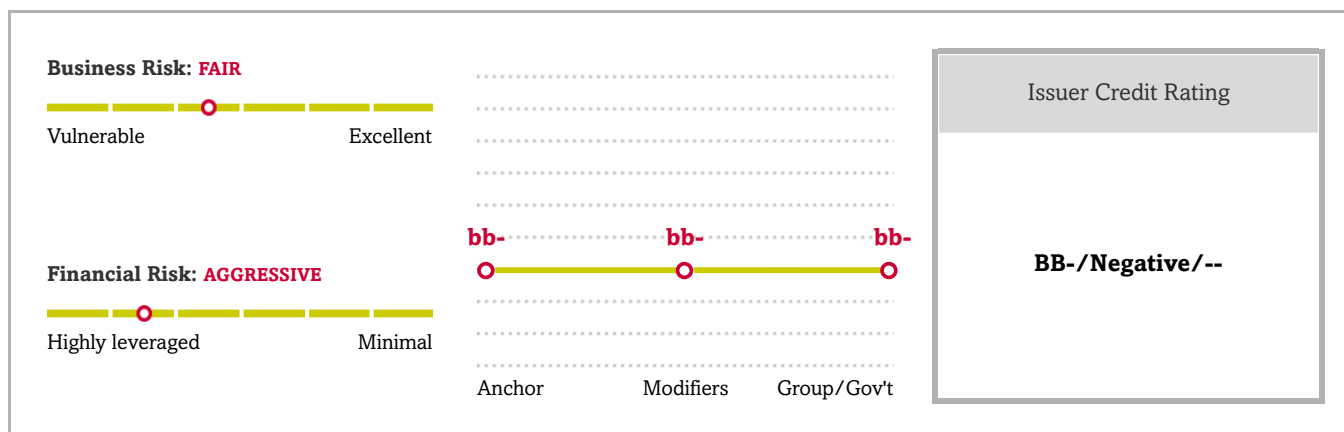
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Arrow Global Group PLC



Credit Highlights

Overview	
Key strengths	Key risks
Solid position in the European market for distressed debt, focusing on profitable, niche assets across its core markets of the U.K., Portugal, the Netherlands, Italy, and Ireland.	Track record of relatively high leverage for the rating level, which is under further pressure across our forecasts as a result of portfolio impairments and cash flow pressure in 2020.
Robust prospective cash flow generation, supported by an increasingly diversified revenue base, likely lower portfolio purchases over the next 12 to 24 months, and improved cost control.	Further underperformance in 2021, likely as a consequence of the tough macroeconomic environment from the pandemic, could precipitate a negative rating action.
Low weighted average cost of debt continues to support the group's financial profile despite difficult operating conditions in 2020, and into 2021.	Capital-intensive business model, with the majority of cash income coming from distressed debt business today.

We expect Arrow Global Group PLC's (Arrow) financial risk profile to deteriorate in 2020, with 2021 seeing a degree of normalization. Arrow has seen a significant shortfall in its collections during the year to date, and S&P Global Ratings does not expect this to abate over the remainder of the year. As a consequence, we expect the group's S&P Global Ratings-adjusted gross debt to EBITDA to exceed 6.5x under our base case for 2020. We expect leverage and coverage metrics to slide back toward historical values into 2021, but to remain above our previous base case.

Our rating on Arrow is supported by a stable and supportive level of liquidity for the next 12 months. Following the completion of the group's second asset-backed securitization (ABS) in the third quarter of 2020, and the full draw of the group's revolving credit facility (RCF), we expect Arrow to have sufficient liquid resources to weather the next 12 months, when operational performance will be below par. This supportive liquidity position is bolstered by the increase in headroom under its RCF covenant package after the group restructured it with its partner banks.

Arrow appears well-positioned to take advantage of the growing market for distressed debt in Europe. Despite the volatile asset performance in the first nine months of 2020, Arrow had £1.7 billion of estimated remaining collections (ERC) at Sept. 30, 2020, and had roughly £56 billion of assets under management on its servicing platform at the end of 2019, a solid presence in the European market. This strategic position will be further bolstered by the deployment of its inaugural pan-European nonperforming loan fund, Arrow Credit Opportunities, starting in 2020 and accelerating over 2021, which we expect to begin to deliver a diversified revenue base, and sustainably lower capital deployment over the medium term.

Outlook: Negative

The negative outlook indicates that the weak economic climate and operating conditions induced by the pandemic will continue to depress the company's cash flow generation and credit metrics. We expect credit ratios to remain weak in 2020, but we also expect Arrow's strengths to be sufficient to weather these temporary difficulties, as we expect ratios to recover in 2021 from 2020 lows.

Downside scenario

We could consider lowering the rating on Arrow if we saw an acceleration in underperformance in the group's core markets over the next 12 months, following an already tough first half of 2020. Importantly, if our expected EBITDA interest coverage (on a cash-adjusted basis), which we currently see as a strength compared with peers, underperforms our base case for 2020, or does not improve significantly into 2021 from 2020 lows, we would likely lower the rating by one notch.

Upside scenario

We could revise the outlook to stable if we see evidence that collections and asset quality are back in line with historical levels, and that the macroeconomic environments in Arrow's core markets will stabilize over the next 12 months. This implies, for instance, capacity to bring leverage metrics in 2021 back to levels close to those in 2019, alongside robust EBITDA interest coverage.

Our Base-Case Scenario

Based on our understanding of information shared by management, Arrow has seen a meaningful deterioration in its performance year to date, and the group does not expect lost collections to be fully recovered. On top of this expectation, the group has overlaid a conservative macroeconomic base case, under which prospective recovery on portfolios has diminished materially. As such, management has elected to report a material impairment of £134 million over the first nine months of 2020, well above the rest of the sector. As of the third quarter, the group had reported no change to this approach.

Our revised base case for 2020 is based on the following key assumptions:

- Cash collections from portfolios to fall approximately 20% from 2019 for full-year 2020;
- Cash EBITDA for the group to be down by more than 20% for 2020 against 2019 levels;
- Break even to negative statutory EBITDA;
- Modest capital deployment of £100 million-£120 million in 2020; and
- Deeply negative statutory earnings for 2020. Tangible equity remains negative for the group, reflecting significant goodwill on balance sheet and our forecasted loss across 2020.

Arrow Global Group PLC--Key Metrics*

--Fiscal year ended Dec. 31--			
(Mil. £)	2019a	2020e	2021f
Debt/EBITDA (x)	3.8	>6.5x	>4.5x
Debt/EBITDA* (x)	9.9	Negative	>10x
EBITDA interest coverage (x)	5.9	>4x	>5x
EBITDA interest coverage* (x)	2.3	Negative	>2x
Debt to Tangible Equity	Negative	Negative	Negative

a--Actual. e--Estimate. f--Forecast. *All figures adjusted by S&P Global Ratings.

Collections shortfalls in 2020 are not likely to be fully recovered in 2021. Under our base case, and in line with management's expectations, we do not expect lost collections in 2020 to be completely recovered in 2021 or beyond. As such, although leverage and coverage will improve after a challenging 2020, we expect this to be to levels higher than previously forecast.

Non-cash-adjusted performance and tangible equity will be negative in 2020. We expect deeply negative net earnings for 2020 to weaken an already negative tangible equity position for the group, which reflects significant goodwill and intangibles on balance sheet.

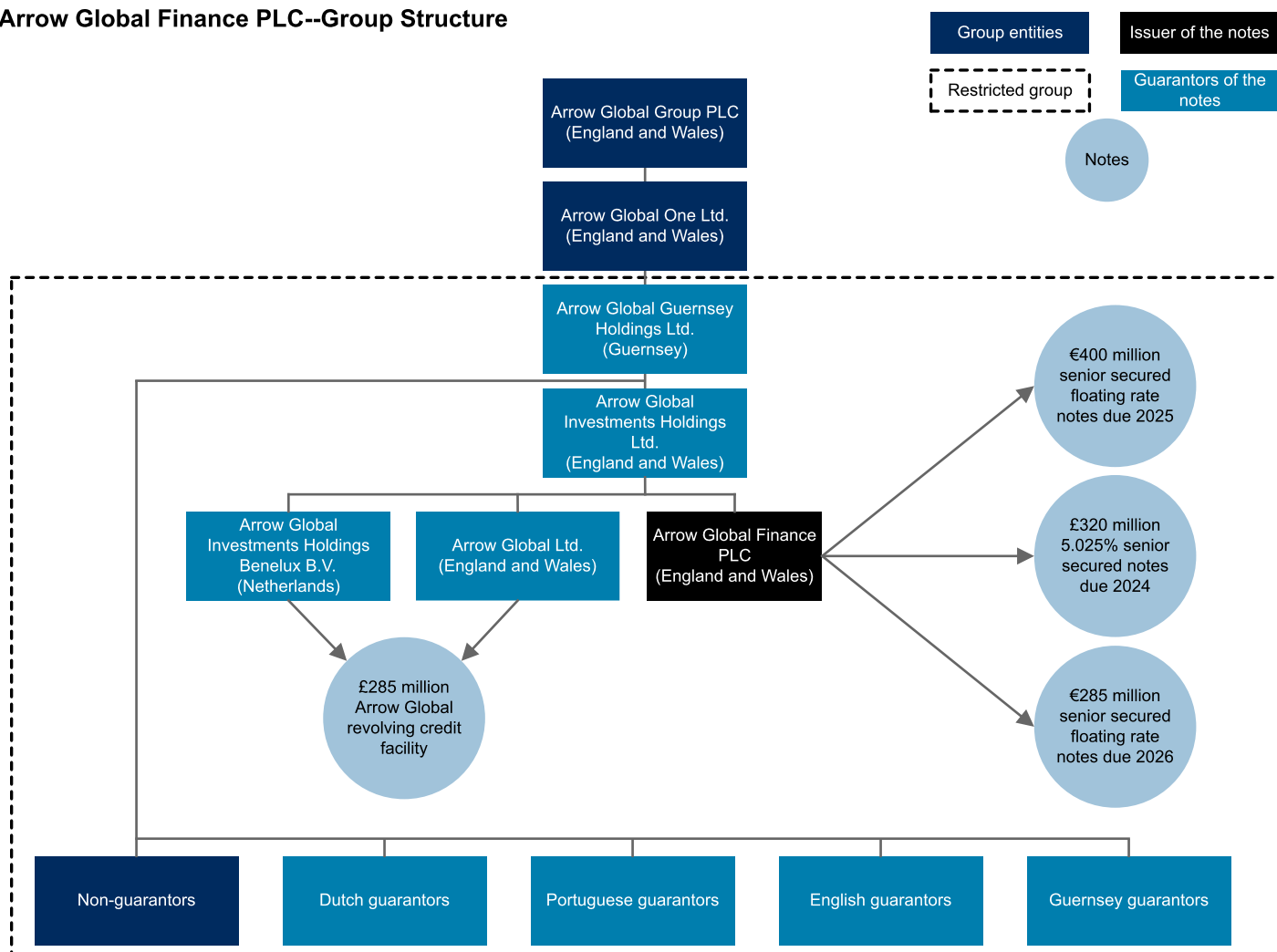
Modest portfolio acquisitions, and a cancellation of the full-year dividend should support liquidity. We expect Arrow to have modest liquidity uses for full-year 2020. Our base case assumes that portfolio purchases will remain low at £100 million-£120 million, and that dividends will be suspended.

Company Description

Founded in 2005 and headquartered in the U.K., Arrow Global is a listed nonoperating holding company that consolidates the activities of the group. Its activities include those performed by operating subsidiaries Arrow Global Ltd., Arrow Global Portugal Ltd., Arrow Global Investments Holdings Benelux B.V., and debt-issuing entity Arrow Global Finance PLC (see chart 1). Our ratings on Arrow Global reflect the credit profile of the consolidated group and our view that there does not appear to be a material barrier to cash flows from the operating subsidiaries to the holding company.

Chart 1

Arrow Global Finance PLC--Group Structure



Source: S&P Global Ratings.

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Peer Comparison

Table 1

Arrow Global Group PLC--Peer Comparison

--Fiscal year ended Dec. 31, 2019--

(Mil. £)	Arrow Global Group PLC	Intrum AB (publ)	Garfunkelux HOLDCO 2 S.A.	B2Holding ASA
EBITDA	324.4	768.5	452.9	341.2
FFO	266.1	586.1	295.1	261.3
Debt/EBITDA (x)	3.8	5.5	5.5	3.0
FFO/debt (%)	21.4	14.0	11.8	25.5

Table 1

Arrow Global Group PLC--Peer Comparison (cont.)				
--Fiscal year ended Dec. 31, 2019--				
(Mil. £)	Arrow Global Group PLC	Intrum AB (publ)	Garfunkelux HOLDCO 2 S.A.	B2Holding ASA
EBITDA interest coverage (x)	5.9	5.5	2.6	5.0

FFO--Funds from operations. * Reporting currency of Swedish Krona, converted to GBP at 12.37 kr/GBP ** Reporting currency of Norwegian Krona, converted to GBP at 11.64 NOK/GBP. Source: S&P Global Ratings database.

Business Risk: Fair

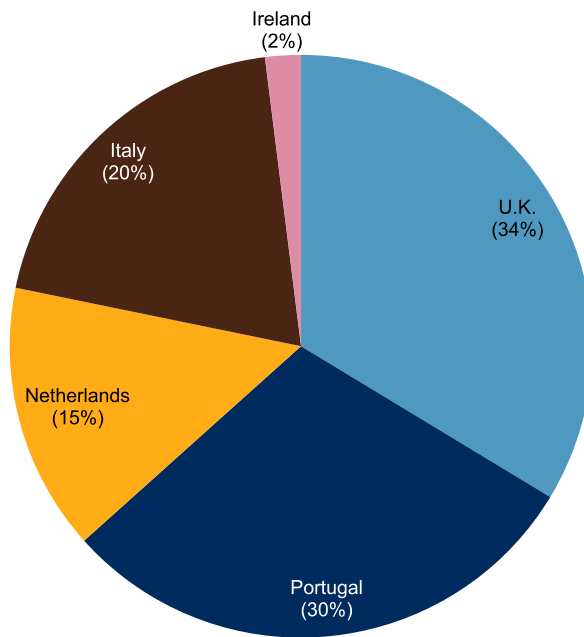
Our view of Arrow's business risk weighs our favorable view of its strategic position in the European distressed debt market--especially its embedded, closely regulated, and mature platform business across its five core geographies--against its narrow focus in a volatile and competitive sector. Furthermore, Arrow is smaller than its largest peers in the European market and has a shorter record of diversification.

Historically, Arrow has focused on U.K. nonperforming loans, but following a series of acquisitions across Europe, it has diversified its cash flows and capital deployment. The largest of these acquisitions were two Italian entities--Parr and Europa Investimenti--in March 2018. The group's most recent transaction was the more-modest acquisition of legal services firm Drydensfairfax in 2019. In 2019, the U.K. accounted for about 30% of Arrow's 2019 capital deployment and Italy for almost 50% of capital allocation.

This transition to a more-diversified front book is borne out in charts 2 and 3. The distribution of the group's estimated remaining collections (see chart 2) reflects Arrow's history of U.K. capital deployment in the back book, while 2019's capital deployment, of which roughly 70% was outside the U.K., speaks to an increasingly diversified front book (see chart 3). We expect to see most capital will be deployed away from the U.K. in future.

Chart 2

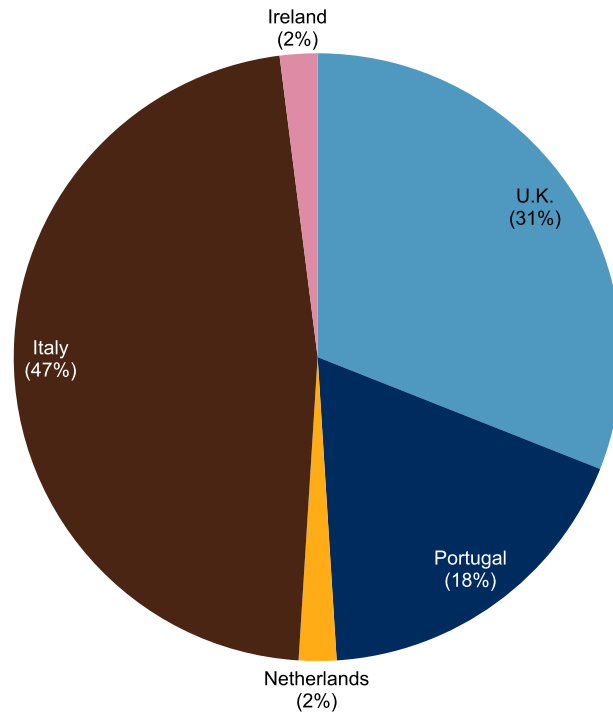
Arrow's 2019 Estimated Remaining Collections Shows Its History Of Capital Deployment In The U.K.*



*84-month estimated remaining collections as at Dec. 31, 2019. Source: S&P Global Ratings. Copyright © 2020 by Standard & Poor's Financial Services LLC. All rights reserved.

Chart 3

Arrow's 2019 Capital Deployment Has Shifted Away From The U.K.*

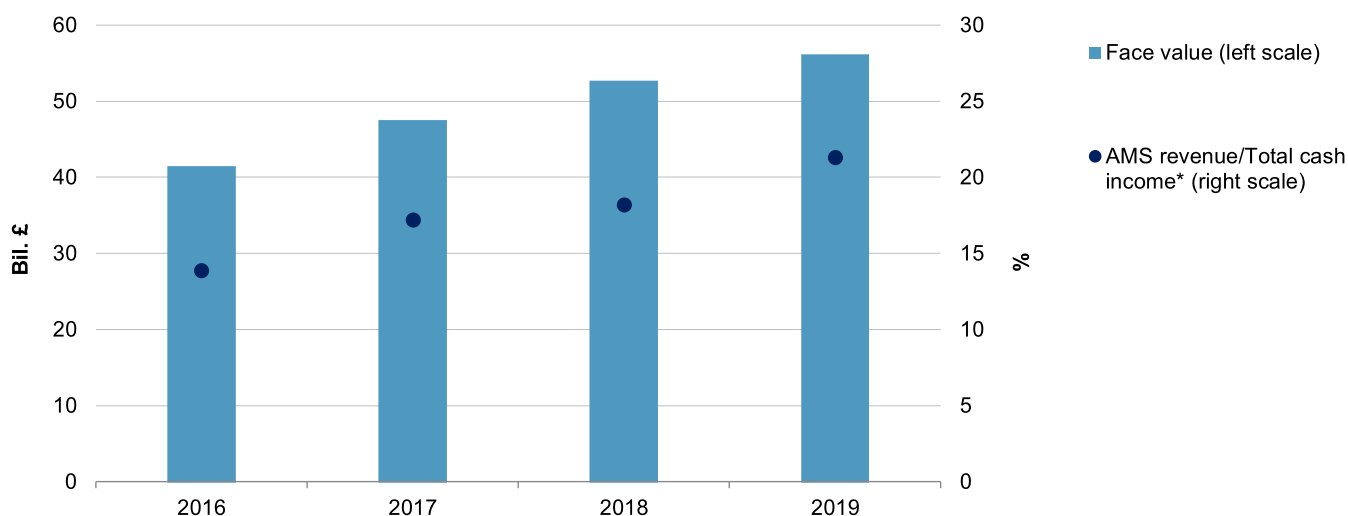


*Allocation of 2019 capital allocation by geography. Source: S&P Global Ratings.
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In a similar vein, the group's asset management and servicing (AMS) business line accounted for above 20% of total cash collections at Dec. 31, 2019, reflecting a concerted period of strategic expansion into this space for Arrow. The group has stated that it intends AMS to contribute about 50% of group EBITDA by 2025, and we expect this line to accelerate its growth as the fund management business deploys more of its available capital.

Chart 4

Arrow's AMS Business Continues To Grow



*Values exclude intracompany transactions. Source: S&P Global Ratings.

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Arrow's fund management business will become a key source of revenue diversification and financial flexibility in future. It was first launched under the Arrow Credit Opportunities fund in December 2019. At launch, the group had €838 million of total capital, which included capital committed by Arrow of €210 million. By the time the fund closed, its total commitments had grown to about €1.7 billion, of which €1.3 billion came from third-party investors.

We would not expect this to materially boost revenue until late 2022, given that, bar modest deployment in 2020, the majority of capital will not be deployed until 2021. However, we would expect the group's revised capital deployment policy, under which it will only deploy capital alongside the Arrow Credit Opportunities fund, to have a more meaningful impact on the group. Specifically, we would expect this policy to keep deployment significantly lower than before, at nearer £200 million. In our view, Arrow will be more able to sustainably cover this amount from operating cash flows.

Despite the group's emerging strengths, we still regard Arrow's geographic and revenue diversification as relatively limited compared with its rated benchmark peers, such as Intrum, Garfunkelux (commonly referred to as Lowell Group), or B2Holding. Intrum, the highest rated peer we cover, is not only diversified across practically all material markets in Europe, it also generates more than 40% of cash revenue from its servicing business. Conversely, although B2Holding does not have material diversification by revenue line, it is well diversified across more than 20 geographies.

In this context, Arrow's lower diversification, and shorter track record in some geographies and lines of business than its peers, could lower the resilience of its business model.

That said, we do not view geographic diversification as credit-positive for its own sake. Some of Arrow's peers are withdrawing from noncore markets, where they have found it difficult to price assets correctly.

Financial Risk: Aggressive

Our view of Arrow's financial risk profile balances our expectation that its financial position will deteriorate in 2020, against our base-case forecast that Arrow's metrics will recover through 2021, supported by the group's low cost debt stack, and conservative capital deployment.

At year-end 2019, Arrow's adjusted leverage sat at 3.8x, broadly in line with our previous forecast of 3.8x-4.0x.

As noted above, at half year 2020, Arrow disclosed an impairment on its portfolios of £134 million. Underpinning this, the group disclosed impairment of 11% of estimated remaining collections in the U.K., 12% in Portugal, 10% in Italy, and 20% in The Netherlands. These shortfalls are broadly in line with our April 2020 base case, though the recorded impairment is slightly ahead of expectation. This approach is largely out of step with rated peers, which have taken a less cautious approach, and as such the scale of impairment is well above many market peers.

To offset the stressed collections experience, the group has disclosed solid cost control, and outlined its commitment to control overheads further under its revised business plan--although we don't expect to see any benefit from these actions in 2020.

We do not expect the group to access the bond market for further leverage over the next 12 months. Indeed, Arrow's capital stack is already well-diversified by maturity, and it has a low weighted average cost of debt.

We forecast headline metrics for the group as follows in 2020:

- Debt to adjusted EBITDA of greater than 6.5x on a cash adjusted basis;
- S&P Global Ratings-adjusted EBITDA to interest expense of more than 4x; and
- Negative tangible equity.

We assess these metrics as being in line with an aggressive financial risk profile, balancing weaker leverage and capital metrics against robust interest coverage for the rating level.

Financial summary

Table 2

Arrow Global Group PLC--Financial Summary						
	--Fiscal year ended Dec. 31--					
	2019	2018	2017	2016	2015	2014
(Mil. £)						
EBITDA	324.4	285.1	228.9	214.1	155.4	101.9
FFO	266.1	231.2	175.6	161.5	110.5	73.5
Net income from continuing operations	37.3	30.0	39.9	26.3	31.7	18.3
Debt	1,241.5	1,205.0	955.0	787.3	530.5	423.9

Table 2

Arrow Global Group PLC--Financial Summary (cont.)						
--Fiscal year ended Dec. 31--						
	2019	2018	2017	2016	2015	2014
Adjusted ratios						
Debt/EBITDA (x)	3.8	4.2	4.2	3.7	3.4	4.2
FFO/debt (%)	21.4	19.2	18.4	20.5	20.8	17.3
EBITDA interest coverage (x)	5.9	5.7	5.1	4.3	4.2	4.6

FFO--Funds from operations.

Reconciliation**Table 3****Reconciliation Of Arrow Global Group PLC Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. £)**

--Fiscal year ended Dec. 31, 2019--							
Arrow Global Group PLC reported amounts							
	Debt	Shareholders' equity	Revenue	EBITDA	Operating income	Interest expense	S&P Global Ratings' adjusted EBITDA
Reported	1,218.0	197.4	339.5	124.3	105.8	54.6	323.0
S&P Global Ratings' adjustments							
Cash taxes paid	--	--	--	--	--	--	(14.0)
Cash taxes paid - Other	--	--	--	--	--	--	--
Cash interest paid	--	--	--	--	--	--	(44.3)
Lease liability	23.5						
Nonoperating income (expense)	--	--	--	--	0.1	--	--
Noncontrolling interest/minority interest	--	4.5	--	--	--	--	--
Revenue - Finance/interest income	--	--	0.1	0.1	0.1	--	--
EBITDA - Portfolio Amortisation	--	--	--	197.5	197.5	--	--
EBITDA - Foreign exchange gain/(loss)	--	--	--	1.0	1.0	--	--
EBITDA - Other income/(expense)	--	--	--	0.1	0.1	--	--
EBITDA - Other	--	--	--	1.4	1.4	--	--
Total adjustments	23.5	4.5	0.1	200.2	200.3	0.0	(58.3)
S&P Global Ratings' adjusted amounts							
	Debt	Equity	Revenues	EBITDA	EBIT	Interest expense	Funds from operations
Adjusted	1,241.5	201.9	339.6	324.5	306.1	54.6	231.2

Liquidity: Adequate

Based on Arrow's likely sources and uses of cash over the next 12 months, we view the company as having adequate liquidity. We expect sources of liquidity will exceed uses by at least 1.2x in the coming 12 months.

In the third quarter of 2020, Arrow strengthened its liquidity position by closing a new €100 million asset-backed securitization, its second such facility. This funding is incremental to the group's existing cash position at the half year of £167 million. This solid cash position is supported, although to a modest extent, by the group canceling its full-year 2019 dividend of approximately £15 million.

Principal liquidity sources	Principal liquidity uses
<ul style="list-style-type: none"> Cash generation from the group's investment and AMS businesses. Accessible cash of more than £200 million, reflecting the full draw on the RCF, and the new securitization. 	<ul style="list-style-type: none"> Portfolio purchases of about £100 million-£120 million; and Modest amortization on the group's existing securitization facility.

Covenants

The supportive liquidity position is bolstered by increased headroom under its RCF covenant package, which the group restructured with its partner banks during the first half of 2020. The previous 4.4x net debt to EBITDA maintenance covenant, which would have fallen to 4.2x by year-end 2021, under this package has now fallen away, replaced by a more flexible quarterly adjusted leverage covenant. Although the previous covenant and Arrow's headroom with respect to it did not constrain our rating, the almost-certain breach of this old and now removed covenant in 2020, and potentially through 2021, would have been a rating weakness. The increased headroom under the RCF covenant also supports the current 'BB-' issuer credit rating.

Issue Ratings - Recovery Analysis

Key analytical factors

- The issue rating on Arrow's senior secured notes is 'BB-', in line with the issuer credit rating. The recovery rating of '3' is supported by the company's asset base, its growing third-party debt servicing capabilities, and our view of the U.K. as a relatively favorable jurisdiction for senior secured creditors.
- Our simulated default scenario contemplates a default in 2025, reflecting a significant decline in cash flow as a result of adverse operational issues; lost clients; difficult collection conditions; or greater competitive pressures, leading to mispricing of portfolio purchases.
- We calculate a combined enterprise value, taking into consideration the different business segments and assuming that Arrow's portfolio of debt receivables would find a potential acquirer. We apply a haircut of 25% to the book value of the debt portfolios. In calculating the assets available to support the group's enterprise value, we deduct the

assets pledged to the asset-based facilities from our estimate of the net portfolio. We assume these facilities to be 100% drawn at the point of default.

- In addition, we assume earnings from its third-party servicing businesses will decline and apply a valuation using a 4.0x EBITDA multiple. We assess Arrow on a going-concern basis, given its long-term contracts and established relationships with customers.

Simulated default assumptions

- Year of default: 2025
- Jurisdiction: U.K.

Simplified waterfall

- Net enterprise value (1) on liquidation: £743 million
- Priority claims (2): £245 million
- Collateral value available to secured creditors: £498 million
- Senior secured claims (2): £946
- --Recovery expectation: 3 (rounded estimate: 55%)

(1)This figure is net of a 5% administrative expense charge. (2)Includes six months of prepetition interest expense.

Ratings Score Snapshot

Issuer Credit Rating

BB-/Negative/--

Business risk: Fair

- **Country risk:** Intermediate
- **Industry risk:** Moderately high
- **Competitive position:** Fair

Financial risk: Aggressive

- **Cash flow/leverage:** Aggressive

Anchor: bb-

Modifiers

- **Diversification/portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Adequate (no impact)
- **Management and governance:** Fair (no impact)

- **Comparable rating analysis:** Neutral (no impact)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Recovery Rating Criteria For Speculative-Grade Corporate Issuers, Dec. 7, 2016
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Corporates | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Financial Institutions | General: Issue Credit Rating Methodology For Nonbank Financial Institutions And Nonbank Financial Services Companies, Dec. 9, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Principles Of Credit Ratings, Feb 16, 2011

Related Research

- Arrow Global Group Issue Rating Lowered To 'BB-' On Significant Impairment; Issuer Rating Affirmed, Aug. 27, 2020
- Ratings Actions On Eight European Distressed Debt Purchasers Reflect Tough Environment For The Sector Amid COVID-19, April 15, 2020
- Europe's Distressed Debt Purchasers In 2020: Growing Out Of Trouble Or Running To Stand Still?, Feb. 03, 2020
- Arrow Global's First Fund Changes Its Strategic Trajectory, But Leverage Pressure Remains, Dec. 19, 2019

Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	Intermediate	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

Ratings Detail (As Of December 2, 2020)*

Arrow Global Group PLC

Issuer Credit Rating BB-/Negative/--

Issuer Credit Ratings History

15-Apr-2020 BB-/Negative/--

01-Aug-2016 BB-/Stable/--

09-Sep-2015 B+/Stable/--

Sovereign Rating

United Kingdom AA/Stable/A-1+

Related Entities

Arrow Global Finance PLC

Senior Secured BB-

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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