Private debt finds its moment in Asia

New funds are attracting some of the world's biggest investors to Asian private credit.

When, in September, the Ontario Teachers' Pension Plan agreed to invest $350 million with Edelweiss Alternative Asset Advisors to put into Indian private credit, there was a sense of Asia's industry finding its voice.

Private debt has for years been a story of potential rather than action in the region; one of the world's gold-standard investors putting serious money not just into India but into a strategy that includes distressed assets in India is a landmark.

It is part of a rising trend.

This year, despite (or maybe because of) the backdrop of Covid, raisings have included $200 million for a private credit fund by Pierfront Capital in Singapore; $500 million by OCP Asia for a direct lending fund for Asian small and medium companies; a new mezzanine infrastructure debt programme for Asia by AMP Capital; and, in October, the formal launch of Edelweiss's $900 million ESOF III private credit fund, within which much of the Ontario Teachers mandate will be deployed.

Other investors in the Indian fund include Florida's State Board of Administration and Swedish national pension fund AP4.

"Some of the leading investors in the world are investors in this fund," Edelweiss group CEO Rashesh Shah told Euromoney and others in an October briefing, "allowing us to capitalize on the credit opportunities in India."

Dislocation

"India has been a robust credit market, but in the last two years it has been hugely disrupted," Shah says. "There has been a large amount of dislocation, and the largest part of that has not just been credit costs going up as the economy slowed down, but asset-liability mismatch issues."

That is creating opportunities for funds that can advance capital on a private basis, "where long-term and patient capital is required. We think the fund format is going to be the best one."

It's not just in India.

Michel Lowy of Hong Kong-based SC Lowy, one of the leaders in the private debt field in Asia, sees opportunity. Not only are there far fewer private credit funds in Asia than in Europe and the US, there is also a much smaller high yield bond market, China being the only meaningful exception.

The number of deals we are negotiating is exploding

MICHEL LOWY, SC LOWY

“That means there are some quality corporates in the mid-cap space that need support,” he says. “There are very few places where they can find that support, and we are trying increasingly to fill that gap.”

What Lowy is talking about is not venture capital; he looks for companies at a certain stage of maturity, demonstrating positive cashflows, with a track record of working well with their stakeholders, and ideally some hard assets.

SC Lowy is looking at transactions in India, South Korea, Indonesia and Australia, among other places, committing its own capital, and then syndicating some of its exposure to co-investors, including some of the region’s sovereign wealth funds.

Sovereign funds in the region known to have a sophisticated interest in private debt including Australia’s Future Fund, the Government of Singapore Investment Corporation and the Korea Investment Corporation.

“From January to August, things were very slow,” Lowy says. “But since then, the number of deals we are negotiating is exploding.”

Momentum

Successful names do exist in private debt in Asia: ADM Capital has been investing since 1998, with a private credit focus since 2004, and has invested in 122 private deals in 16 countries in the region, deploying $2.96 billion of capital and exiting 104 deals.

But names such as ADM, SC Lowy and Edelweiss have been outliers. Now there is a sense of new momentum.

The existence of a bankruptcy code is a huge plus because it does change the culture of credit

RASHESH SHAH, EDELWEISS

The research group Preqin says that the number of private debt investors in Asia has gone from 115 in 2014 to 477 at the end of 2019, with assets under management held by them climbing from $28 billion to $64 billion over the same period.

That’s still far behind the US and Europe, which Preqin says accounted for 96% of the total value of global deals last year, but there is a sense that Covid may have provided opportunities for new entrants.

The Alternative Credit Council said, in a report that was launched in August based on a survey of 28 private credit asset managers in Asia, that there was a $4.1 trillion annual funding gap for Asia’s small and medium-sized companies, which ought to present an opportunity for private credit.

The region offers some considerable advantages: largely healthy government debt-to-GDP levels, a mainly robust response to Covid-19, and a gradual awareness of alternatives to relying on domestic bank funding.

Difficulties

Set against that, Asian private credit markets are far less liquid than those in the US and Europe, which has an impact on cost.

Many companies are family-run, which may lead to complex ownership structures, limited accounting track records, and a need for more careful due diligence, the ACC report says.

Covid has obviously pushed some companies into distress; Edelweiss says it will look at both performing and distressed credit, and Lowy says he is interested in turnaround stories as well as robust companies.

On the distressed side, India captures the most attention, particularly since the implementation of an insolvency and bankruptcy code, which eventually passed its biggest test with the resolution of the Essar Steel bankruptcy, something in which SC Lowy was closely involved.

“The existence of a bankruptcy code is a huge plus because it does change the culture of credit,” says Shah. “It does improve recovery times. We always believed it would take five or six years for the code to stabilize.

“But we think it’s a game-changer.”