EXPERT Q&A

Johnson Har, head of Hong Kong at Alter Domus, Kevin Williams, head of operations for Asia-Pacific, and Jayesh Peswani, relationship manager for Asia-Pacific, offer their perspective on Asian special situations and how investors can access opportunities onshore and in the broader region

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Q How much distressed debt and special situations activity are you seeing beyond Europe and US?

Johnson Har: In Hong Kong we are seeing more direct special situations investment activity. Historically this has been conducted by locally based fund managers focusing on that specific strategy, but we are now witnessing a change in the type of market participants.

Investors are diverting from fixed income hedge funds and instead going into the direct debt area, for example. Additionally, we are aware of a lot more LPs in general becoming interested in the Asia-Pacific region and are looking for managers in this area. There are a lot of discussions going on among people looking to launch a fund in the next six to 12 months.

Kevin Williams: As far as distressed debt goes we are not seeing a very high amount of transactions taking place, but mainland China is getting a lot of coverage over the non-performing loan issue, which is obviously something that foreign investors have a history in. The problem is that the deals being done are conducted in an opaque market and it's difficult to get a handle on the total amount of volumes being transacted. That said, the main issue at the moment is one of supply, and while local and foreign players are setting up platforms to purchase NPLs, they probably wish they could deploy more, but need to be a bit patient to actually put that capital to use.

Q What is driving investors' interest in Asian distressed debt and special situations?

Jayesh Peswani: News stories, such as the recent ramp up in the trade war between US and China, suggest that some companies will soon start to feel the pinch. When that happens, you will start to see more deals taking place. This means that those investors who have already raised capital are either actively investing, or instead circling around some of these companies, waiting for activity to pick up. It's one of those markets where it is really hard to figure out what exactly is happening because the whole strategy of distressed debt managers is to quietly approach potential targets and do the deal before other people find out.

Q What kind of opportunities are your clients looking at in markets like Asia?

JH: With the debt market in Asia Pacific having more depth and breadth, investors are getting more comfortable and it's no longer seen as a niche product. And it's not just first-time debt funds, but also other firms which have raised these types of funds before or are looking to expand their other fixed income strategies into that area. Real estate is certainly one of them, whether it's NPLs or special situations. Chinese real-estate developers need more flexible sources of capital, be it domestic or international in origin.

Outside of China we are definitely seeing credit opportunities with real estate as well. Whether it's a mezzanine player just getting more money than they could from the banks, or unusual situations with collateral, there is often a real estate borrower involved.

Q What are the major challenges when operating in that region when it comes to understanding local markets and the distressed debt opportunities available?

KW: Players in this sector need to become more efficient with their platforms and understand how they are going to coordinate their people on the ground, all the way up to getting a consolidated view across a portfolio they have purchased. While the market is maturing in China, investors do need to be more organised and efficient.

Often the fund managers have front-office capability, and they know what they are doing in underwriting credit, but they don't have the type of operational platform a bank would. The software available to manage this is often not tailored to alternative investment managers.

Q From a fund services perspective, what are the specific needs of a client operating in Asia?

KW: While it not something that we cover, sourcing deals is probably the main constraint when we talk to our clients. A lot of them could raise more capital, but it's a case of deploying it in Asia. LPs want exposure to these markets but it is more of a matter of how many deal opportunities there are out there. Once firms do find an opportunity they want to take, it's rare that there is a fully operational platform for the fund to handle all the aspects of the investment properly in-house.

Another issue is that the opportunity may be unique and that involves a lot of paperwork. Then it is a question of coordinating the workflow across a team. It's tough to do that in Excel, and difficult to manage these portfolios from a distance. In many cases, when firms buy those portfolios in different geographies, they must be local to capitalise and convert those NPLs into cash.

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Q How significant is the greater diversity of Asian markets relative to their European and US peers when it comes to investing in either distressed debt or special opportunities?

KW: If a client originates or purchases a loan, they often don't have a platform in place. That comes from the market not being very large historically, and this certainly creates some operational headaches. Firms often don't know what opportunities are going to arise, and when they do, they could look very different from what they expected initially. It's sometimes a bit of a scramble operationally to kind of catch up with the investment and make sure they are monitoring it and reporting on it properly.

Q Do you see the Asian market expanding, and to what extent?

JP: If the Chinese market is successful, that will raise interest across the region. Take India, for example. It has become attractive now, and that is partly down to them cleaning up the rules on collecting NPLs. All of this has slowly made people a bit more comfortable with India, but what drives activity in that market is how the economy is performing there at a fundamental level. At a high level it is making progress and it is growing, so there are opportunities there as well.

If you take a look at South-East Asia there is a lot of nuance with each of the markets, so it's very difficult to say what level of opportunity there is. You have activity going through Hong Kong and Singapore, and a lot of it is directed at these markets. Nevertheless, I would say that South-East Asia is still lagging a little bit behind. ■