Investing in Asia Private Credit

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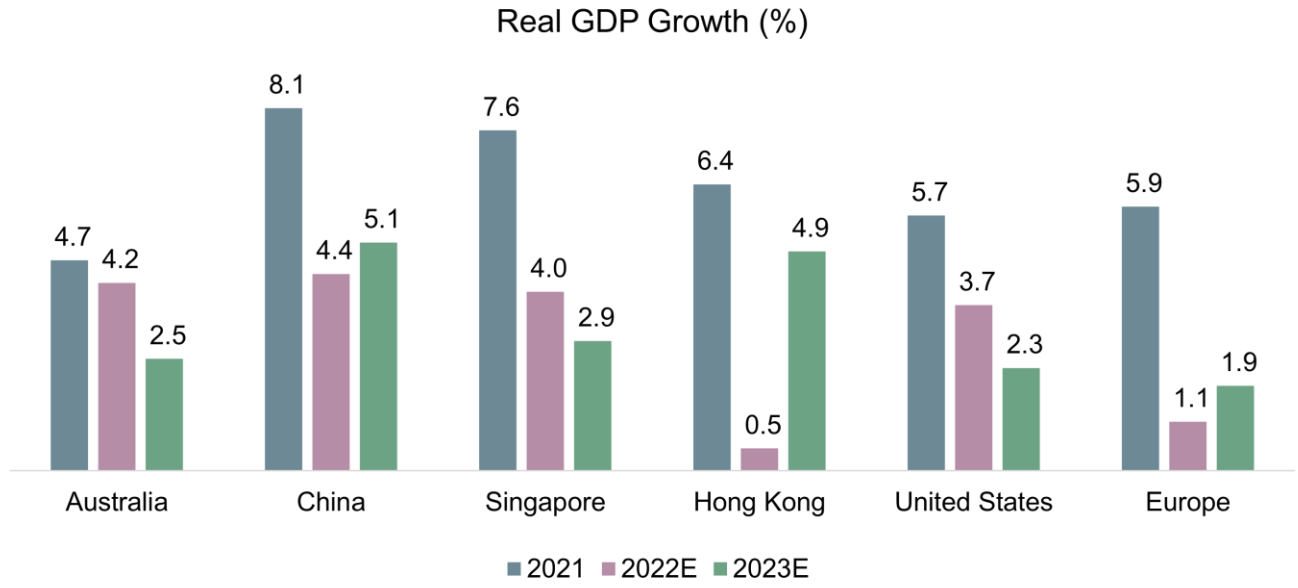
Global allocation to private credit has been gradually increasing due to its resilience against rising interest rates and inflation. Here you'll find out more about how this asset class is trending in Asia.

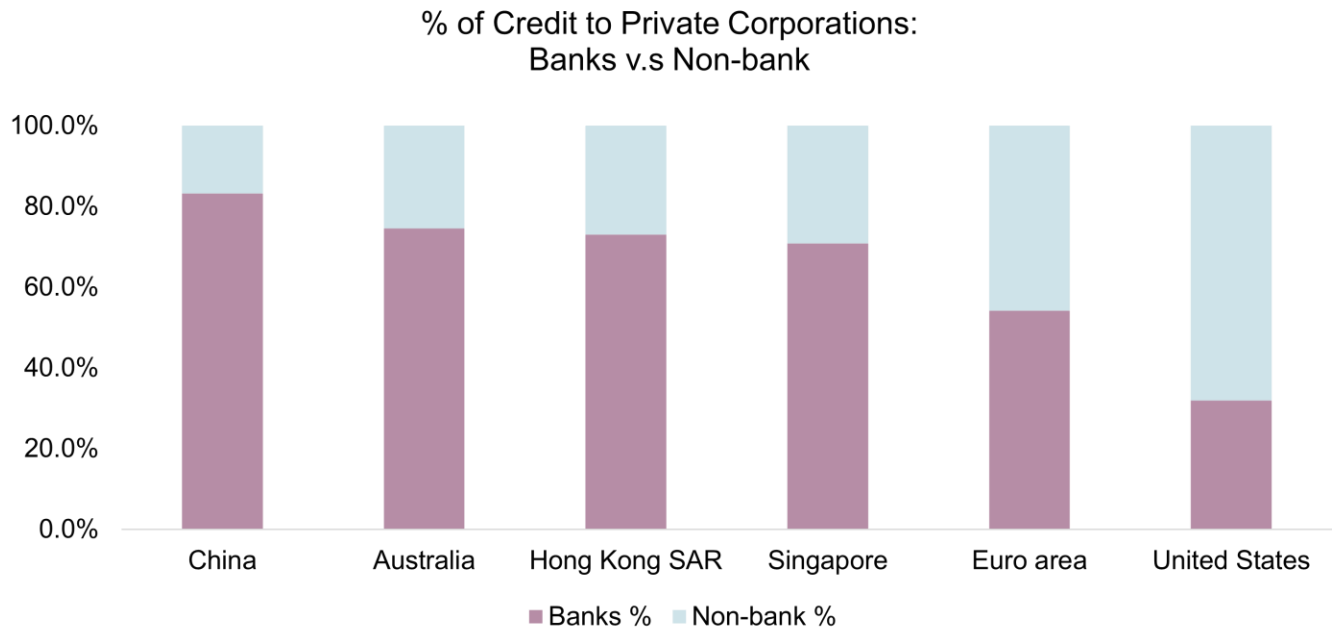
Why Private Credit in Asia?

Since the outbreak of the pandemic, Asia remains the world's growth engine and with the gradual easing of travel restrictions in most of the region's economies, an increase in structural financing is observed.

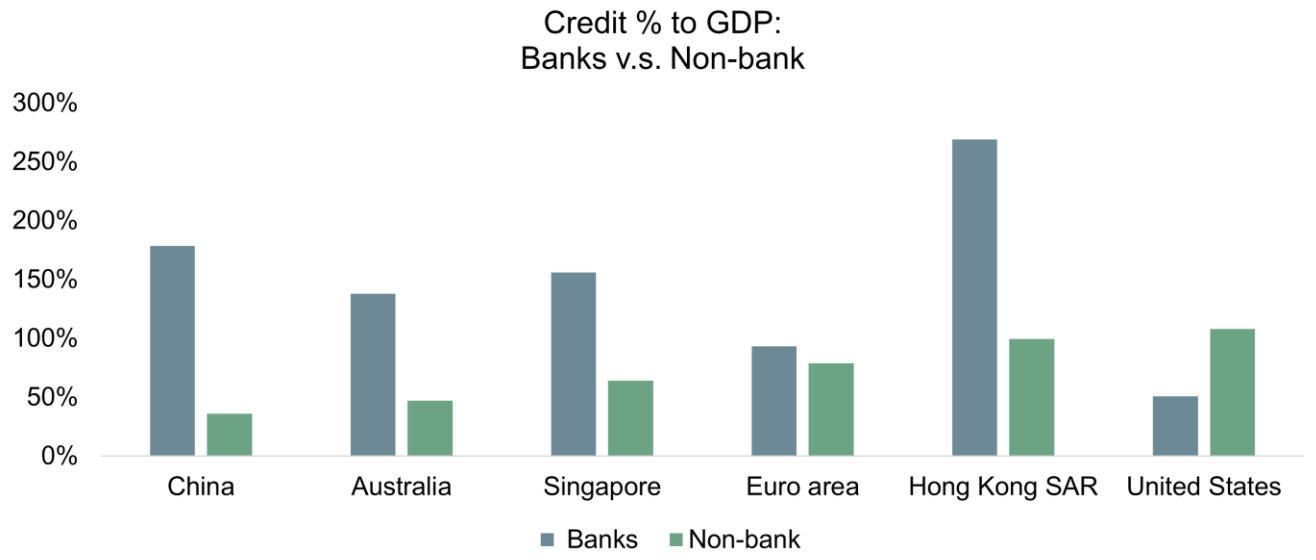


Source: World Economic Outlook, IMF, April 2022

In the Asia-Pacific, private credit is still an emerging asset class as bank financing continues to dominate capital raising.



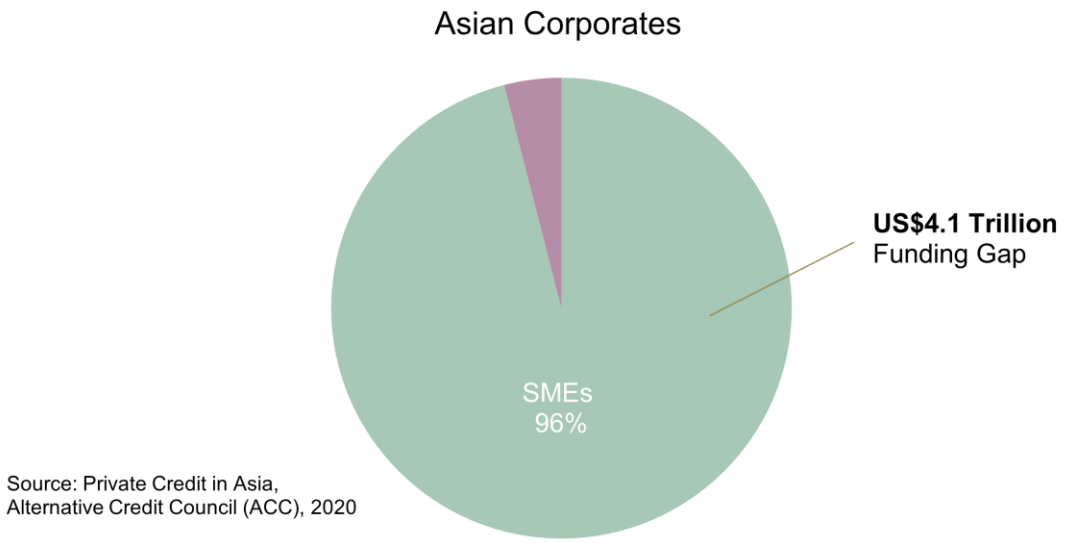
Source: Bank for International Settlements, as of 31 December 2021



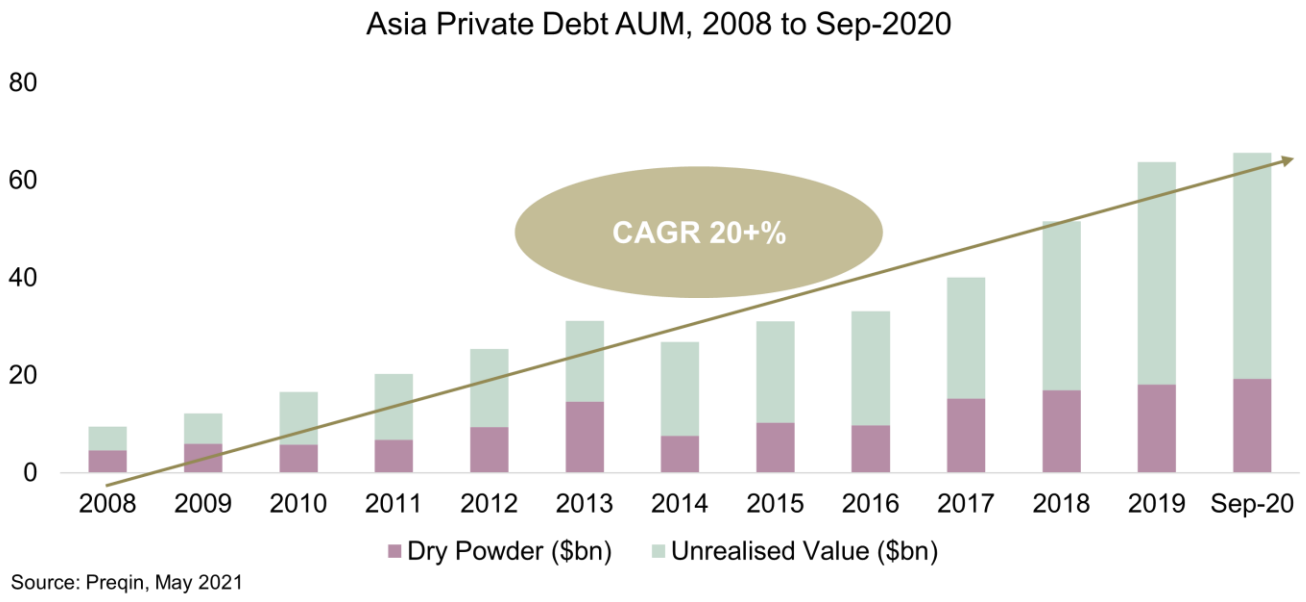
Source: Bank for International Settlements, as of 31 December 2021

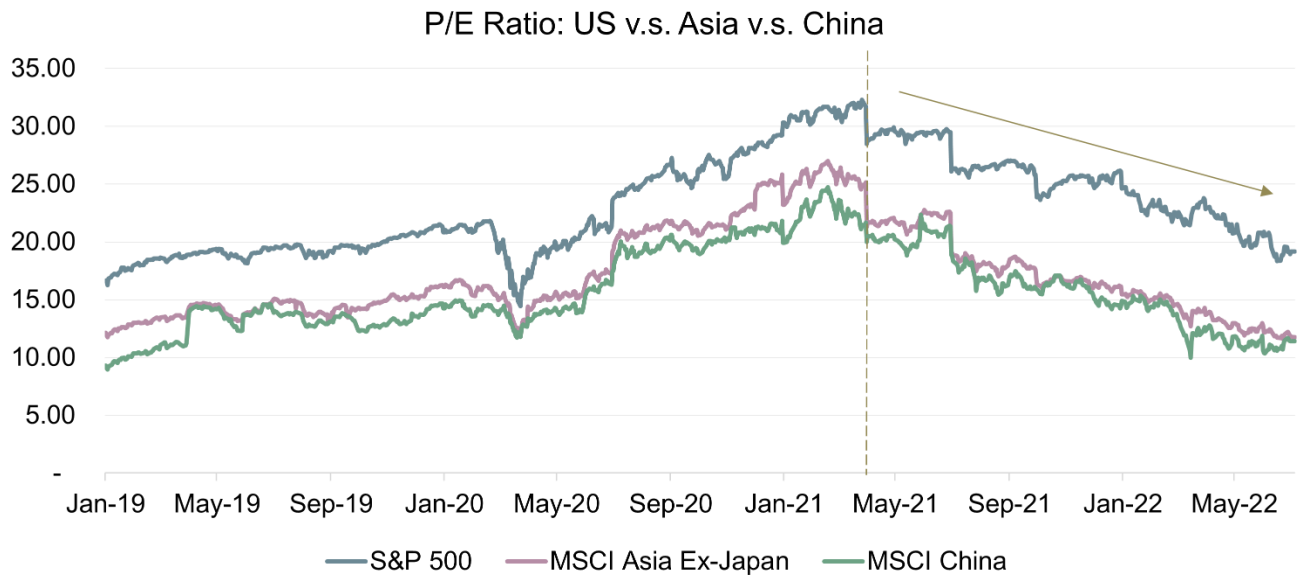
In recent years, however, more lenders have become less willing to issue new loans to Small-and-Medium Enterprises (SMEs) due to a decrease in appetite for risk. The region is experiencing a growing gap between the supply and demand for capital, where private credit as an alternative meets this underserved market segment and narrows funding gaps.

The Alternative Credit Council (ACC) estimates that SMEs account for 96% of all enterprises in Asia and are the main drivers of employment and GDP growth. But because of the rigid financial ecosystem and regulatory environment, they face difficulties securing traditional bank financing. A US$4.1 trillion funding gap for SMEs was estimated in the region in 2019.



Preqin estimates that Asia-Pacific private debt assets under management (AUM) totaled US$65.6 billion in Q3 2020, compared to US$595.6 billion in the US and US$289.5 billion in Europe. The region's private debt AUM has grown at a CAGR of more than 20% since 2008. As in Europe and the US, we expect this trend to continue and pick up even further.





Source: Bloomberg, as of 5 July 2022

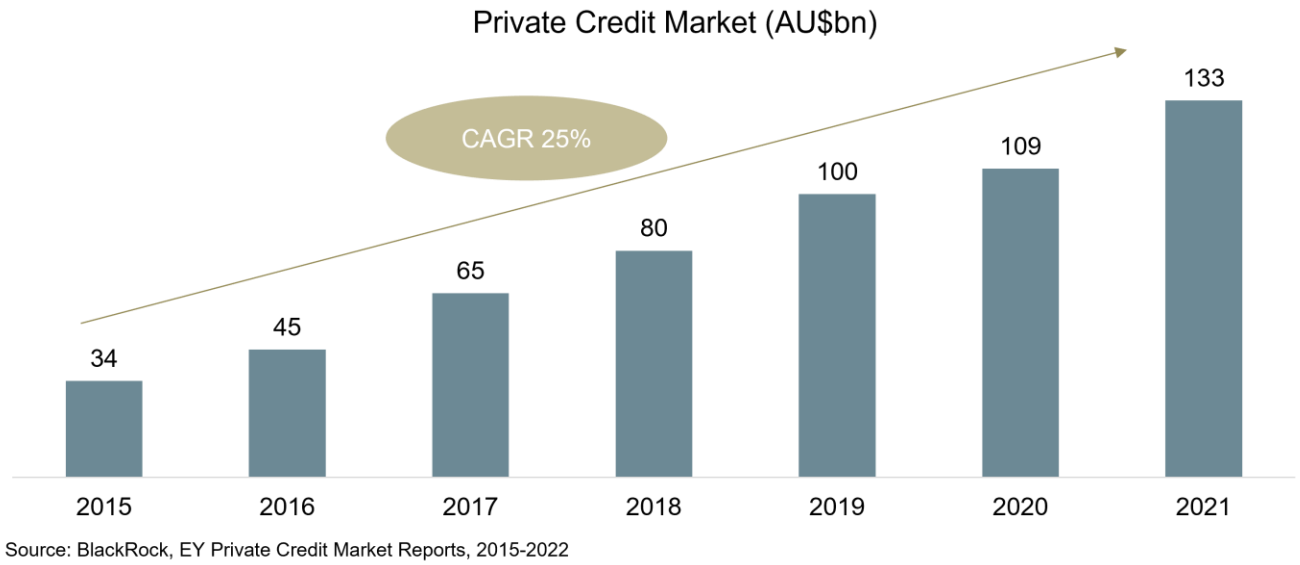
Rising Underlying Fundamental Demand vs. Supply Shortage in the Region

Australia

According to the IMF, Australia's economy will grow by 4.2% this year after recovering from the pandemic. Additionally, the economy is boosted by a low unemployment rate in 50 years, high consumer sentiment, and strong corporate performance.

Traditional retail banks in the country are cautious when it comes to issuing new loans due to the regulatory environment, high capital requirements, and low-risk appetite. Based on the latest report published by EY and Australia Investment Council, non-banking lending contributes AU$1.2 billion to the Australian GDP and supports over 10,000 jobs in the country.

Post COVID-19 outbreak, private credit has played a pivotal role in extending alternative or emergency capital to SMEs, thanks to its flexible structure and negotiable terms. The private credit market in Australia reached AU$133 billion in 2021, or 11% of the corporate and business lending market, up 21% from AU$109 billion in 2020. Over the period from 2015 to 2021, the market remarkably grew at a CAGR of 25%, and we forecast this market trend to carry on.



Hong Kong & Singapore

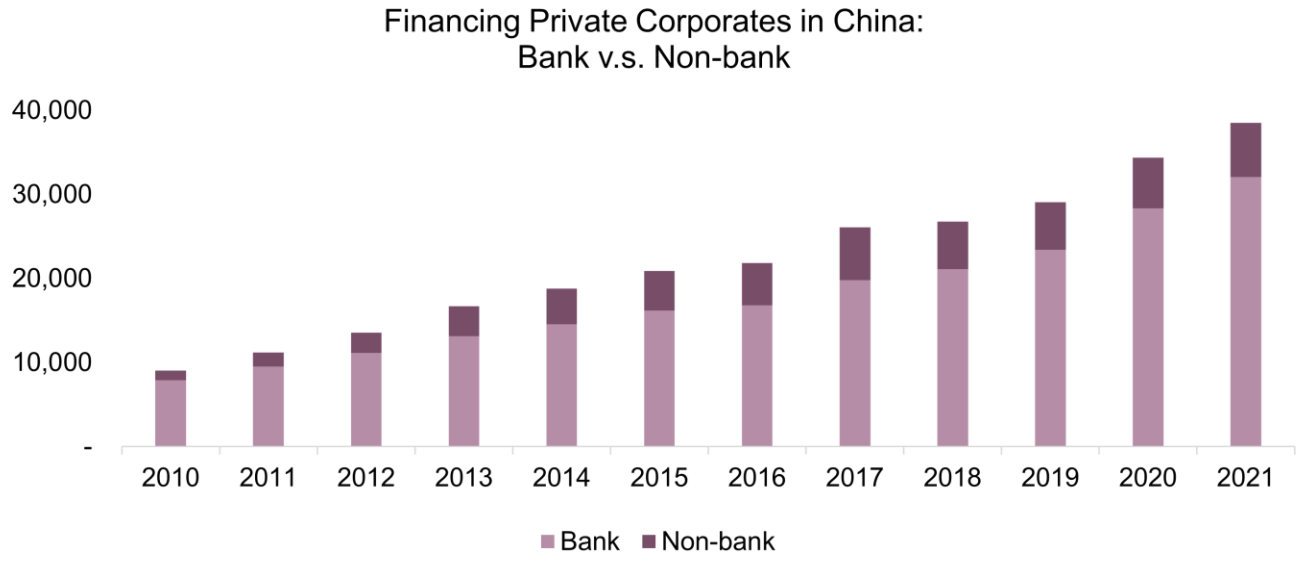
As gateways to Southeast Asia and Greater China, Singapore and Hong Kong have legal and bankruptcy systems similar to developed countries such as the US and UK. It is common for holding companies to be established in these cities while running operations in other developing cities due to their professional workforces, hi-tech setups, and/or tax benefits. Loaning to those companies could enable lenders to take advantage of a well-established legal system while tapping a wider variety of opportunities in the region. Furthermore, due to the increasing dry powder in PE/VC, private debt financing has been preferred over traditional bank loans for flexibility and negotiability.

China

Recently, global investors have been contemplating whether China remains an attractive investment. Our local Petiole team remains confident in the nation's long-term growth potential as China continues to play a dominant role in the outlook for the emerging region.

After a series of lockdowns across the country and the Dynamic Zero-COVID policy during the first half of 2022, eased measures were announced in June, including a shorter quarantine period. Over the next few months, as China's travel restrictions are expected to further be relaxed, its GDP is predicted to grow again with China's relatively low inflation, a favorable monetary policy, and strong exports.

Additionally, SMEs are also seeking private credit to expand due to China's continuing crackdown on shadow banking.



Source: Bank for International Settlements, as of 31 December 2021

As the private credit market sustains growth in the coming years, more investors are anticipated to allocate to private credit strategies for their unique characteristics.

As part of Petiole's diversified private market investment programs, we have been harnessing private credit's potential over the past decade.

Contact our expert team today to find out more about how private credit/debt can be valuable to your investment requirements.

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