ADM's Private Credit Strategy – Predictable and Consistent Performance

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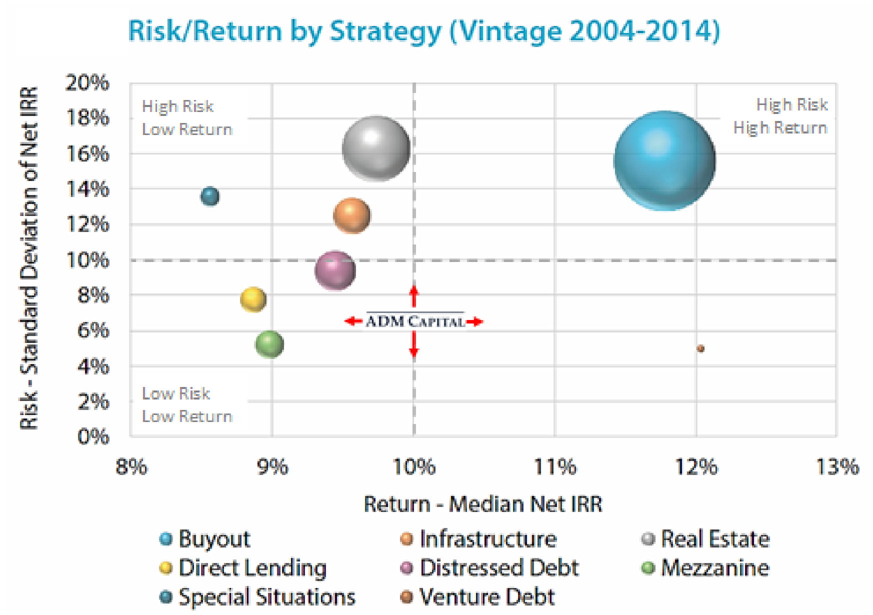
The investing world is currently going through a curious phase. On one hand, the rally in the US equity markets continues undiminished, fuelled by expectations of a pro-business US administration enabling business growth. In theory, this should in turn lead to higher interest rate expectations and an upward shift in bond yield curves; however, notwithstanding the overnight price moves, yields in fixed income and corporate bond markets remain quite compressed, seemingly arguing for a "lower for longer" interest rate environment. Such mixed and continually changing signals therefore adds uncertainty and unpredictability to even the most fundamentally sound investment thesis, with the effects further amplified for emerging markets investors.

In this context, private investments allow a greater focus on corporate fundamentals, enabling investment decisions that are based on (more measurable and predictable) fundamental analysis rather than market expectations. Private credit and private equity have their own unique place in this continuum, depending on investors' needs for income and risk control vs. return. Furthermore, a Private Credit strategy captures numerous sub-strategies that are quite different in the risks they are exposed to and the actual returns they have generated. ADM Capital's current approach to private credit, an outcome of our considerable experience and track record in this space, has ensured consistency and predictability in returns over the past 5 years. Given the illiquidity premium on offer in comparison to public markets, and the relatively higher liquidity compared to private equity, we believe our funds are an ideal tool for diversification in investors' portfolios.

The diagram below, extracted from Preqin, plots the risks vs. the returns of various asset classes, covering over 800 funds globally. Against this, we have mapped ADM Capital risk and return.



Source: Preqin Private Debt Online

One measure of risk is the standard deviation of net IRR over 10 years (vertical axis), while return is defined as the median Net IRR over 5 years (horizontal axis). The size of the bubble indicates the sample size of AUM in that strategy. A few observations:

1) **Volatility varies significantly:** Private credit investment strategies are scattered across the y-axis, suggesting that volatility (ie risk) across individual strategies is quite mixed. For example,

returns for real estate investing is subject to high volatility, so is buyout. Standard deviation of returns in mezzanine and direct lending strategies have been lower – i.e., their returns are more consistent/predictable.

2) **Underachieving lending strategies:** Numerous asset classes are at the left side of the x-axis, suggesting actual returns are below 10% for the last several years. Particularly note the performance of distressed and infrastructure strategies which seem to have higher risk and yet demonstrated lower returns than expected. Particularly of note is the “special situations” asset class – these managers by design, employ flexible mandates including primary, secondary, performing/non-performing credits or even equity. Indeed, this asset class appears to have highest risk and lowest return: per Preqin, the top performing fund achieved net IRR of 61.4% while the worst fund reported -8.7% (June 2016 data), underscoring the variability in returns of this strategy.

3) **ADM Capital’s consistent, secured lending approach:** ADM Capital’s position in this graph is well balanced – our strategies are quite stable and low in volatility while benefiting from higher returns – gross investment returns from our Asian positions in our actively managed portfolios have ranged from 15-17% over the last 5 years. This is mainly due to the following:

- Our positions are in secured debt, oftentimes 1st lien positions in mid-sized companies. In Asia, where creditor priorities and cash flow waterfalls are not always observed in practice, it pays to be in secured debt to limit risk, and equity to maximise returns, while other creditor buckets are somewhat fuzzier in terms of actual risk-return. Indeed, the good bargaining power we enjoy as secured creditors is because we take security over multiple assets that in theory can be foreclosed in the event of default. In practice, we structure our transactions to ensure that borrowers’ interests are aligned with that of ADM Capital, thereby allowing for outcomes based on alignment and ownership rather than litigation.

- Our investments in emerging market debt give us some premium and bargaining power relative to that in developed markets. For instance, a senior secured debt strategy in the US generates around 7-8% net return vs. ADM Capital’s net 10-12% returns (excluding unrealized equity upside which can typically add 1-2%). Demand for credit is strong throughout the region, with increased intra-regional trade, acquisitions, and tourism potential underscoring the need for ongoing specialist financing. We are encouraged by the genuine economic growth displayed by Asia Pacific economies and their mid-market enterprises.

- Our sourcing strategy is key to our performance, in that we source our own deals, which gives us greater control and stronger relationships with our borrowers. As such, our actively investing Asian portfolios have generated 16.9% gross IRR over the past 5 years across all our funds with no defaults. Our Investment Advisory Committee typically reviews more than 250 opportunities per year before ultimately selecting 15-20 of them to structure and invest in. This allows us to be extremely selective in the construction of high quality portfolios.

Investors typically look to the fixed income asset classes to provide income while keeping risks under control. In this regard, we believe that ADM Capital’s approach to private credit investing makes our proposition most attractive from a risk adjusted return perspective, while adding predictability and consistency to performance. Admittedly, our approach is rather more boutique and less scalable than some of the other strategies, however, capacity will grow as both investor appetite and demand for financing increase in the coming years.

Should you have any questions or like to discuss further, please contact Sabita Prakash at sabita.prakash@admcap.com.

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