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Future of private debt: The last word with ADM

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Christopher Botsford, founding partner and joint chief investment officer at ADM Capital, talks about how the private debt opportunity is unfolding in Asia.

ADM Capital is a Hong Kong-based investment manager offering senior secured direct lending and mezzanine debt to mid-market sized companies. Its funds address a credit vacuum in Asia whereby mid-market firms operating in nascent or evolving financial markets cannot gain access to long-term structured debt financing through traditional means.

In private credit, ADM has invested in 116 Asian private transactions in 15 countries, with 101 exits and approximately $454 million of gains since 2004. The largest exposure in its flagship fund is Australia, with just under 15 percent of the portfolio, while the Philippines tops exposure in its emerging markets portfolio, with 35 percent.

What are your key investment markets in Asia, and why?

We don’t have specific asset allocation criteria, but consider individual investments opportunistically across developed markets, core emerging markets and, more recently, the frontier markets of Asia.

In recent years, we have observed a gradual reduction in the correlation between these markets to China and the Western economies. Indeed, some frontier economies like Vietnam and Cambodia are in the boom phase of their capital cycle, notwithstanding the slowdown in China. We believe that investing collectively across these markets provides our investors with diversity and consistency in returns.

How do you see prospects for private debt in Asia?

The global private debt asset class has grown substantially over the last five years. We believe that there is a strategic shift in the offing that is expected to result in significant growth in Asian private debt.

From a demand perspective, we are seeing an increasing number of investors seeking some level of income, as well as consistent, predictable and attractive risk-adjusted returns not hostage to market volatility.

From the supply angle, we are expecting to see the opportunities for financing in our markets proliferate, particularly given that Asia is still witnessing solid economic growth in most markets, while traditional financing channels like banks are unable to keep up given capital constraints.

What do you think will be the key developments over the next few years?

On a relative and absolute basis, Asian private credit is now providing the most opportunity and highest returns. Mid-sized companies, unable to obtain credit from traditional forms, are turning increasingly to the private credit market to obtain essential credit for corporate purposes. Investors alike are seeing this as a viable alternative to public market returns.

Jurisdictional and legal reforms are being put into place across both emerging and frontier economies, making for a more navigable landscape for investors and borrowers alike. As this continues, it follows there will be more service providers attracted to the space making for a more transparent, tradeable and efficacious investment medium.

And what could be the main challenges to the development of private debt?

Lack of homogeneity in different legal jurisdictions adds complexity to analysis and structuring, making scalability challenging. Although private debt strategies have greater exit options than private equity, a number of these options depend on borrowers’ ability to successfully refinance their debt with local banks – at the moment, it is difficult to predict the future shape and size of banking systems.

On the returns spectrum, private credit falls somewhere between high yield bonds and mezzanine funds, but, in reality, is lower risk than either of these asset classes given the first lien collateral that we typically take in return for extending senior secured debt to companies. As such, those investors that have fairly specific asset allocation targets may not be able to slot Asian private credit very neatly into their frameworks.

How do you think regulation may impact the asset class?

Typically, the alternatives industry is relatively lightly regulated since its investors are sophisticated institutions with full knowledge and awareness of the risks involved in these types of investments. Furthermore, it's even less likely that regulation will substantially change specifically for the private debt asset class, since the growth of this asset class has been much more measured and controlled. We believe that the current regulatory environment provides a healthy backdrop within which we are able to provide strong, uncorrelated returns to our investors.

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