privateequitywire

PRIVATE DEBT
IN FOCUS



FEATURING
ALTER DOMUS

www.alterDomus.com

alterDomus*



85% of the world's largest private debt managers place their trust in us

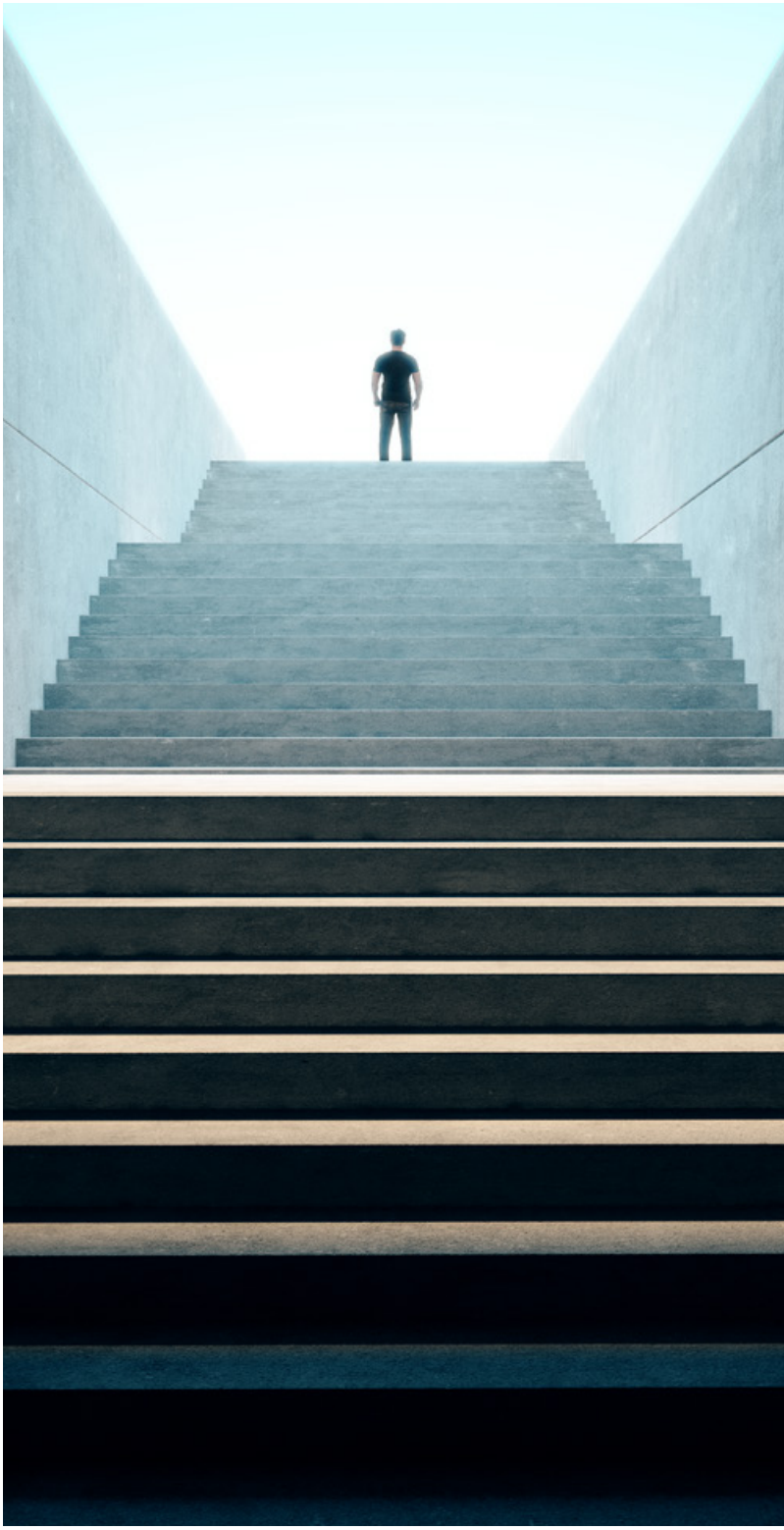
These world-leading debt managers, credit funds and special situations funds rely on our end-to-end outsourced solutions. From loan administration to agency services, our expert teams and platform are built around supporting complex debt strategies of any form. At Alter Domus, we understand the multifaceted world of private debt.

Interested in finding out how our expertise and systems can bring clarity to your complex debt portfolio? Visit our website to find out more and get in touch with a member of our team.

INSIDE THIS ISSUE...

04 **OVERVIEW**
Use of private assets shifts as appetite remains strong

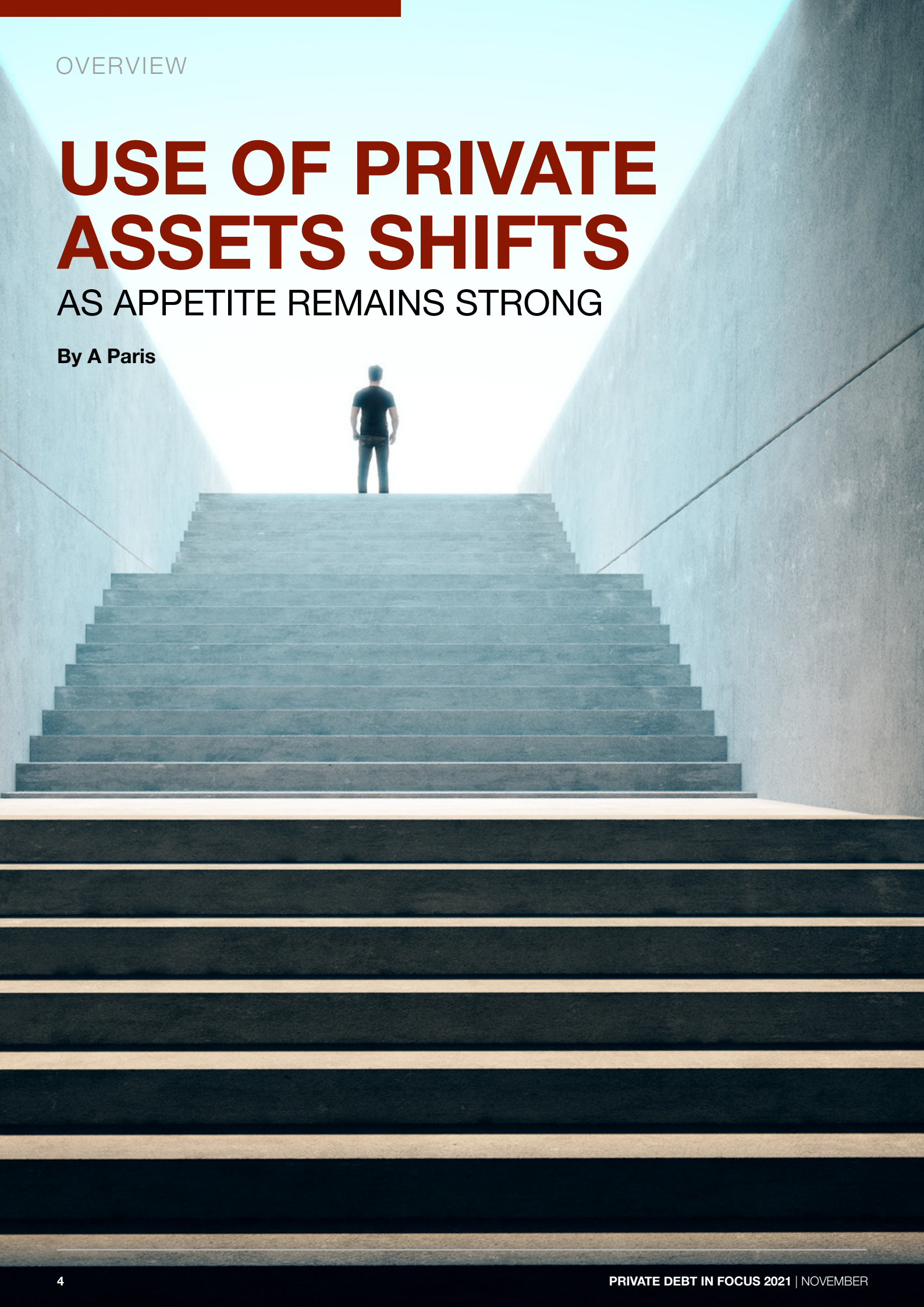
06 **ALTER DOMUS**
Expanding for growth



USE OF PRIVATE ASSETS SHIFTS

AS APPETITE REMAINS STRONG

By A Paris





> Private debt has consistently given investors access to higher returns coupled with lower risk compared to high-yield bonds or broadly syndicated leveraged loans
>
> **Mercer, Asset Management Firm**

Having entered the year with a record fundraising pipeline, according to a report by McKinsey, private debt was set for success in 2021. And the asset class did not disappoint; with strong returns and growing inflows, investors continue to allocate to this sector in search of opportunity, risk mitigation and diversification.

Data from Pitchbook shows that private debt generated a 9.2 per cent in Q1 2021, with preliminary Q2 2021 returns of 9.1 per cent being suggested. Distressed debt, venture debt and infrastructure debt helped push the private debt returns overall to 15.2 per cent, according to the data provider.

"Growth in private debt continues to be fueled by long-term secular trends, in particular, the disintermediation of bank lending channels due to regulatory developments in the wake of the GFC, as well as sustained low interest rates on traditional fixed-income securities due to accommodating monetary policy," details the McKinsey Global Private Markets Review 2021.

BROADER ASSET CLASS APPLICATIONS

Private debt investments can not only act as a diversifier within investor portfolios, but such assets can also form part of a broader cashflow or liability driven investment solution. In this context, this year has seen the asset class being promoted in more depth to pension schemes.

In May this year, BlackRock launched a private debt income fund specifically designed to meet the needs of UK pension schemes. The fund aims to provide investors with a yield premium relative to liquid credit markets, reliable income, and capital preservation.

The asset management giant also revealed the role private markets can play within US public pension plan portfolios. In a study which leveraged data from over 85 public pension plans, the firm outlined the challenge these institutions face, namely: "Liability growth and increasing required benefit payments and put additional pressures on investment portfolios to outperform following periods of market decline, such as during the first quarter of 2020."

According to the study, private assets can offer diversification benefits and help these plans mitigate risks. BlackRock outlines: "The study modeled the potential impact of reallocating 5 per cent of each plan's exposure from public equity to private equity, and found expected returns increased by more than 70 basis points, on average, bringing many plans within reach of their assumed return. Risk increased commensurately, but portfolio efficiency (return per unit of risk) increased by an average of 3 basis points."

In an article, Schroders investment professionals, Jon Exley, Solutions Manager and Clement Yong, Fund Manager, Multi-Asset, explain: "The "real asset" nature of underlying debt in private credit deals, such as infrastructure and real estate, means defaults are typically lower. Infrastructure – think roads, telecommunication networks, schools – tends to be less sensitive to the economic cycle."

FOCUSED STRATEGY

Private debt gained significant momentum in the wake of the global financial crisis, as institutional investors sought to fill the void left by the tightened bank activity.

Asset Management firm, Mercer explains: "Private debt has consistently given investors access to higher returns coupled with lower risk, compared to high-yield bonds or broadly syndicated leveraged loans." In view of this, it follows that investors are showing a strong appetite for the asset class in the current climate, as it offers strong cash yield and return potential, as well as with diversification and risk mitigation benefits.

However, investment selection will be key as the sector comes under growing regulatory scrutiny. Experts at PwC note that investors will "need a strategy that focuses more closely on strategic positioning, operational excellence and capital efficiency in their business and the portfolios they manage." ■

EXPANDING FOR GROWTH



Private markets have been growing almost exponentially over the last 10 years. As banks have pulled back from lending with regulations starting to bite, more private asset managers have put together lending strategies to replace what the banks traditionally provided in the market.

COVID CORRECTION

There was a sense that Covid-19 might provide a correction to this growth, especially as it has been 13 years since the last correction. Greg Myers, Group Sector Head – Debt & Capital Markets at Alter Domus, a leading provider of integrated solutions for the alternative investment industry, says: "Everyone thought that Covid would be that event that would lead to a lot of defaults and restructurings, but because of the government stimulus and wanting to keep nearly every industry in place to avoid a cataclysmic shock, that cycle hasn't started yet."

He adds: "Once the government stimulus slows down, it's likely to show some cracks. It's going to be interesting to see what happens."

Since 2020, Alter Domus has seen a number of clients launch special situations and credit opportunities in anticipation of the expected reset in the market and increasing levels of default. However, the firm hasn't seen a lot of those funds being deployed as of yet.

Myers comments: "It's been very interesting to watch how resilient a lot of these borrowers are. The demand for performing loans and the yield that comes from them is so strong that I don't think there's necessarily the appropriate level of risk priced into some of these assets."

NEW MARKETS, NEW OPPORTUNITIES

As Myers points out, opportunities in the private markets vary region by region. In Asia, for example, banks are still the principal lenders, remaining resilient in terms of how they lend and the companies they lend to. Consequently, there are less private credit opportunities in the region than in Europe and North America, for example.

"It is difficult to have a perspective on Asia, because Japan and Korea are very developed capital markets, as are Singapore and Australia to some extent. But the banks are very involved and have a lot of capital. Where they don't, they still have a good regulatory framework," Myers comments.

In Europe, by contrast, banks are cautious about expanding their footprint, and even US banks are adopting a more thoughtful approach to company lending. Myers says: "In North America, the middle and lower-middle markets have a lot of significant private lenders, with armies of originators across the country that are meeting with companies and putting that into place, whether lending to a company that's well-positioned to acquire a competitor coming out of Covid-19 or lending to a private equity firm that wants to create a dividend situation for a privately held company. There is a lot of capital in the private debt market."

Myers particularly notes a rebound in oil and gas, but also venture and technology firms that would typically have relied upon private equity. "They have now decided that they'd rather borrow for their capital needs and not dilute their equity prior to IPO or being acquired," he adds.

BUILDING A FUND SERVICES ECOSYSTEM

As the markets begin to rebound from Covid into some version of a 'new normal', there is the associated challenge of building a fund services ecosystem to facilitate growth, product development, new sectors and new markets.

One of the principal issues across the sector and beyond is a profound shortage of talent and competition between financial services firms for a shrinking pool of staff.

"The technological demands of our clients continue to increase, and the reporting and delivery methodologies for providing data to our clients is always front of mind, but getting the right resources, talent and systems in place is a challenge, not just from an accounting and loan operations perspective, but also from the lack of IT professionals," says Myers.

Alter Domus had addressed some of the need for staff and for clients' tech demands through recent acquisitions. In December 2020, the firm acquired IPS Fund Services, a Boston-based fund administrator serving private equity and venture capital funds, to



expand its North American presence. This was followed by Utah-based Strata Fund Solutions, cementing Alter Domus' position on the West Coast. And June 2021 saw the firm continue its rapid US expansion with the acquisition of New York-based IEA.

Myers comments: "This gives us a great suite of services where we can go to our clients and offer not only the traditional middle and back office services that we normally provide, but also credit monitoring tools, waterfall carry tools, and all sorts of other things; it augments our existing offering quite well."

Such rapid expansion creates challenges too, in terms of getting different systems and staff onto the same platform, but Myers is confident that expanded tech and geographic offering will meet clients' needs. With what he calls "the great resignation" impacting custodian banks and trust banks, to the extent that some are pulling back on services or even firing clients, Alter Domus is well-positioned to take advantage.

Myers says: "It's not that we want to be all things for all people, but we want to offer a very focused and thoughtful approach to cover any alternative market. I'm optimistic as we head into the winter and into 2022; there's a lot of opportunity for growth," he adds.

MEETING ESG NEEDS

Like so many other sectors of financial services, private debt is being impacted by the drive towards ESG-compliant investing; and naturally, fund administrators must move to meet its clients' needs in this field.

Alter Domus is developing an ESG product which will assist in regulatory reporting disclosures and asset level reviews. The firm has also elected to align to The World Economic Forum (WEF) 'Measuring Stakeholder Capitalism; Towards Common Metrics and Consistent Reporting of Sustainable Value Creation' framework.

"Getting the right attributes at the right frequency and level of detail to satisfy the ESG requirements has been an interesting challenge. We're at very end stages of the offering, and there's certainly a lot more attention in the EU," Myers says. ■



GREG MYERS

GROUP SECTOR HEAD, DEBT CAPITAL MARKETS, ALTER DOMUS

Greg Myers is responsible for shaping Alter Domus' strategy for lenders and debt fund managers globally and overseeing business relationship management for Alter Domus' North America fund administration group. As an experienced Financial Executive, Myers has over 15 years of broad-based financial services expertise. Previously, Myers managed the Specialty Bank Loans team within LaSalle Bank's Global Securities and Trust Services group and acted as an equity options market maker at the Chicago Board of Options Exchange. He additionally worked as a financial analyst and Y2K consultant with other financial institutions.

alterDomus*

www.alterdomus.com

Many leading international asset managers, lenders and asset owners choose Alter Domus as their partner for growth. Our talent pool of more than 3,300 employees across 36 offices in 21 countries combined with cutting-edge technology work to put our clients ahead of the game. Dedicated to serving private equity, real assets and debt capital markets sectors, we offer fund administration, corporate services, depositary services, transfer pricing, capital administration, domiciliation and management company services. Our extensive experience in the debt capital markets sector allows us to provide specialist solutions such as loan administration, agency services, trade settlement and CLO manager services.

privateequitywire