UPDATE

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Fund Finance Association Executive Committee 2024 APAC Market Update - Top Takeaways

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The Fund Finance Association Executive Committee recently hosted the APAC 2024 fund finance update, featuring insights from market commentators, legal practitioners, and lenders on the fund finance landscape.

The discussion covered perspectives on the Hong Kong, Singapore, Australia, and Japan markets, as well as the broader alternatives market. Participants also shared valuable insights from both lender and offshore viewpoints. Below is a summary of the top takeaways from the session.

Private capital

The private capital market has faced challenging fundraising conditions in recent years, which have continued into 2024. APAC-focused funds and fundraising have hit a decade low, however, private capital globally is still forecast to grow at 10 per cent annually over the next five years.

In APAC, investor sentiment towards private equity and private credit remains strong, as well as other income-focused asset classes such as infrastructure and real estate.

India is the most favoured emerging market, with a steadily growing private credit fund base of around US$21 billion. According to Preqin, 48 per cent of investors see India as presenting the best opportunities among emerging markets.

Fund and fund finance market update

- Lenders: over the past 12 months, the lender base has become more concentrated in APAC, but lenders are still comfortable to put facilities in place because investors have shown strong conviction for reputable sponsors and fund managers. Facilities have included structural enhancements such as investor acknowledgment letters or comfort letters from initial limited partners (**LPs**). Established methodologies for capital calls are becoming increasingly important for banks – European and US banks already have these methodologies in place so APAC borrowers should be aware of this trend. Additionally, there is a growing focus on disclosure requirements.
- Customisation and innovation: LPs are increasingly requesting customised structures, both in terms of fund structures and documentation. This trend presents both challenges and opportunities for innovation within the industry. A heightened focus on specific strategies, regions, or Environmental, Social, and Governance (**ESG**) criteria has resulted in a rise in separately managed account (**SMA**) transactions, a trend that is anticipated to persist over the coming year. Additionally, the market is seeing the introduction of bespoke facilities, including those compliant with Islamic Shariah law.
- ESG: Once a peripheral concern, ESG has become a core issue, driven by LP demands and regulatory crackdowns on greenwashing. Managers are increasingly focused on ESG, however, the cost and time required to implement these policies is significant. ESG-linked subscription facilities are emerging in APAC, although their volume remains higher in the US and EU.
- Net Asset Value (**NAV**) and hybrids: The current climate has made asset divestment more challenging, leading to an increase in continuation funds and a subsequent rise of NAV facilities in deal flow. There

is a growing global appetite from non-bank lenders, positioning the NAV market in APAC for growth. Lenders are equipping themselves with both NAV and hybrid lending policies.

- People: The market is seeing a growing talent pool of fund financiers. The launch of the Fund Finance Association University this year underscores the increasing interest and engagement in the fund finance industry. Those keen to learn more should look out for the events run by the NextGen Network scheduled for later this year. Details of the events will also be mailed out to the NextGen mailing list in due course.

Greater China and Hong Kong market update

The private capital fundraising environment in Hong Kong is experiencing significant challenges, with record low levels of activity and no clear signs of a turnaround in the Chinese real estate market. Larger sponsors in the region are not seeing substantial fundraising, and there is a decline in the availability of large subscription line facilities. Geopolitical factors are also impacting the market, leading to relatively flat deal flow. However, there is a high volume of refinancing and renewal activity for existing "plain vanilla" subscription line financings, despite an increase in pricing.

Clients of the collapsed Silicon Valley Bank are still actively seeking alternative financing solutions, with market participants working to fill this void. SMAs have become increasingly active, with rising deal volumes as investors assert more specific requirements and greater influence over transaction terms. Additionally, event-driven fund financing is emerging as an innovative use case for subscription line facilities.

Despite the subdued overall market activity, lenders remain highly engaged and continue to seek out new opportunities. The private capital market is demonstrating resilience and maintaining a positive long-term outlook.

Singapore market update

Singapore has continued to experience steady economic growth, maintaining a robust start to the year. However, investor sentiment has been tempered by persistent global conflicts, rising interest rates, and increased regulatory scrutiny of local family offices and hedge funds. The Monetary Authority of Singapore has also imposed stricter regulatory and reporting requirements for investment funds.

Despite these challenges, the Singapore private capital market has seen several positive developments. Notably, global alternative asset manager Blackstone has doubled the headcount of its private equity business in Singapore; while BlackRock launched its largest Singapore-focused exchange-traded fund to date, targeting Asian companies committed to reducing carbon emissions - a sign of growing investor interest in sustainable investing. Furthermore, Singapore's sovereign wealth fund, Temasek, closed a US$1.4 billion fund with a focus on decarbonisation initiatives.

The Singaporean market has also seen an increase in investment into AI and financial technology. Transactions with a sustainability-linked component have also gained traction, although there is disparity in the real monetary benefit. Capital call facilities have maintained their popularity, while NAV-based facilities have proven more difficult to price, dependent on the underlying security and asset structure.

Australia market update

In line with global trends, Australia has experienced a slowdown in fundraising activities, particularly when it comes to new subscription facilities. Despite this slowdown, there are still refinancings, extensions, and post-investment period financings being executed.

Capital call products continue to dominate the market, particularly gaining traction among newer and smaller managers. However, given the largely bilateral nature of the market, it remains challenging to quantify and compare these trends with those in the US or European markets. NAVs have long been a staple of the Australian market and therefore, unlike in other parts of the world, they do not exhibit the same growth trajectory. They remain a critical component of the financial landscape.

Interestingly, while the number of deals has dropped, the aggregate capital raised by funds in Australia has actually increased, indicating a sense of cautious optimism in the market. Credit funds are actively raising; meanwhile GPs are establishing continuation funds to retain and increase asset values amid a challenging exit market. The market could benefit greatly from more exits and IPOs to inject energy and open new opportunities.

Japan's emerging fund finance market update

Despite Japan's status as a developed country, it is considered an emerging market in the context of fund finance. The market shows substantial demand and interest, particularly for funds involving foreign vehicles in their structures (such as Cayman Islands and Singapore). However, there are a number of challenges. Firstly, Limited Partnership Agreements (**LPAs**) in Japan typically contain model language that prohibits borrowings, rendering them 'un-bankable'. Efforts are currently underway to modify these LPAs to make them viable for financing.

Secondly, fund structures in Japan often involve multiple parallel vehicles due to tax and regulatory considerations, which complicates the overall structure and creates additional hurdles for financing. Lastly, security and collateral perfection approaches in Japan differ from those in the Cayman Islands and Singapore. This requires lenders to take additional time to become comfortable with the process.

Despite these challenges, there is significant interest from both Japanese and non-Japanese lenders in financing funds. Fund formation levels are particularly high in Japan, particularly in buyout, real estate, infrastructure, and credit funds.

Cayman Islands perspective

Fundraising in the APAC region has faced challenges over the past year, but the total average number of Cayman Islands fund launches saw a modest increase in 2023. There is growing interest in tech-focused funds, real estate funds, infrastructure funds, and venture capital funds.

Similar to other regions, there is a demand for bespoke financing structures in APAC. Some private credit lenders are entering the market to offer NAV, GP and management facilities, and private credit is also being used to restructure distressed portfolio companies through fund finance facilities. However, these bespoke structures can be costly and are not always economically viable.

Japan, in particular, is showing increased interest in utilising Cayman Islands fund structures, with notable and positive market activity observed.

Summary

Despite facing geopolitical headwinds and challenging macroeconomic conditions, industry leaders in the APAC region remain optimistic about the resilience and growth of the fund finance market. Investor sentiment is positive about fund finance, and lenders are committed to supporting the market.

It is forecast that fund finance will gain more momentum starting in 2025, with capital raising projected to achieve year-on-year gains. Flexibility and innovation will be crucial for sustaining future growth in this sector.

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