

Supporting NPL Securitization/Distressed Asset Funds - The ADB Perspective -

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Introduction

ADB: Participating at early stage

- Public Sector: Advising policy and framework dialogue, coordination and relationship management with Governments
- Honest broker in negotiating NPL sales
- Private Sector: Debt and Equity funding at early, riskier, stage – catalyze other investors, demonstration effect

ASIAN NPL MARKETS: Developing & Risky

- Early stage: Thin market, fewer players, limited experience
- Limited public data on profitability



Recent trends in investment banking

Ramping up proprietary business

- shrinking investment banking fees
- growing proprietary trading
- expanding distressed debt investment business
- example: Goldman Sachs's business model in Japan

Growing advisory business in area of distressed assets

Bond funds not attractive when interest rates at bottom

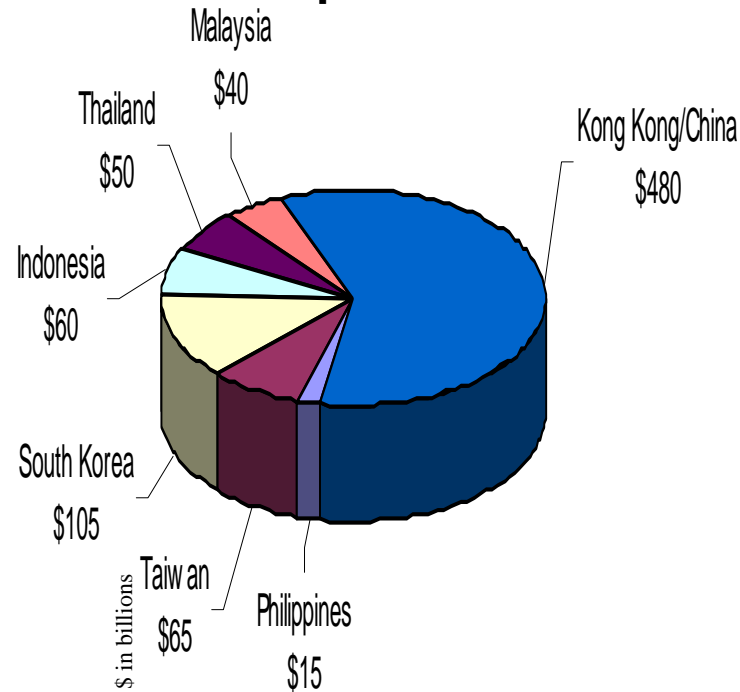
Distressed Asset funds – gaining attention

Asian NPLs - Magnitude is large

- Country limits and single deal exposures for investors
- Exit through the stock markets not possible in all countries (Philippines, Indonesia).
- Fair Market Valuations are difficult – limited ability to benchmark transaction
- Increasing sophistication from sellers (e.g. PRC AMCs): role of SOCBs

Total Magnitude of Distressed Debt

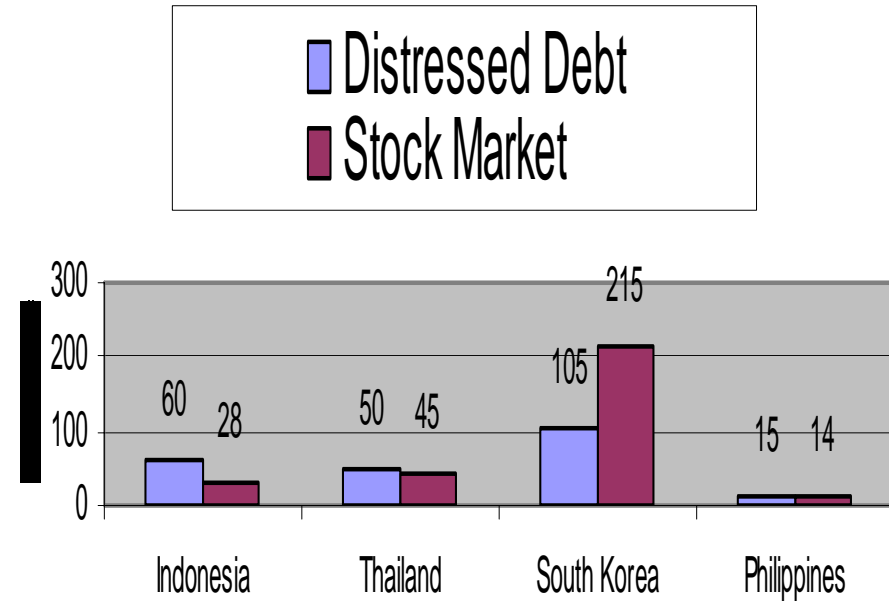
Total Asia ex-Japan Distressed Debt



Source: Ernst & Young; Bloomberg

- Approximately US\$815 billion of Asia ex-Japan NPLs

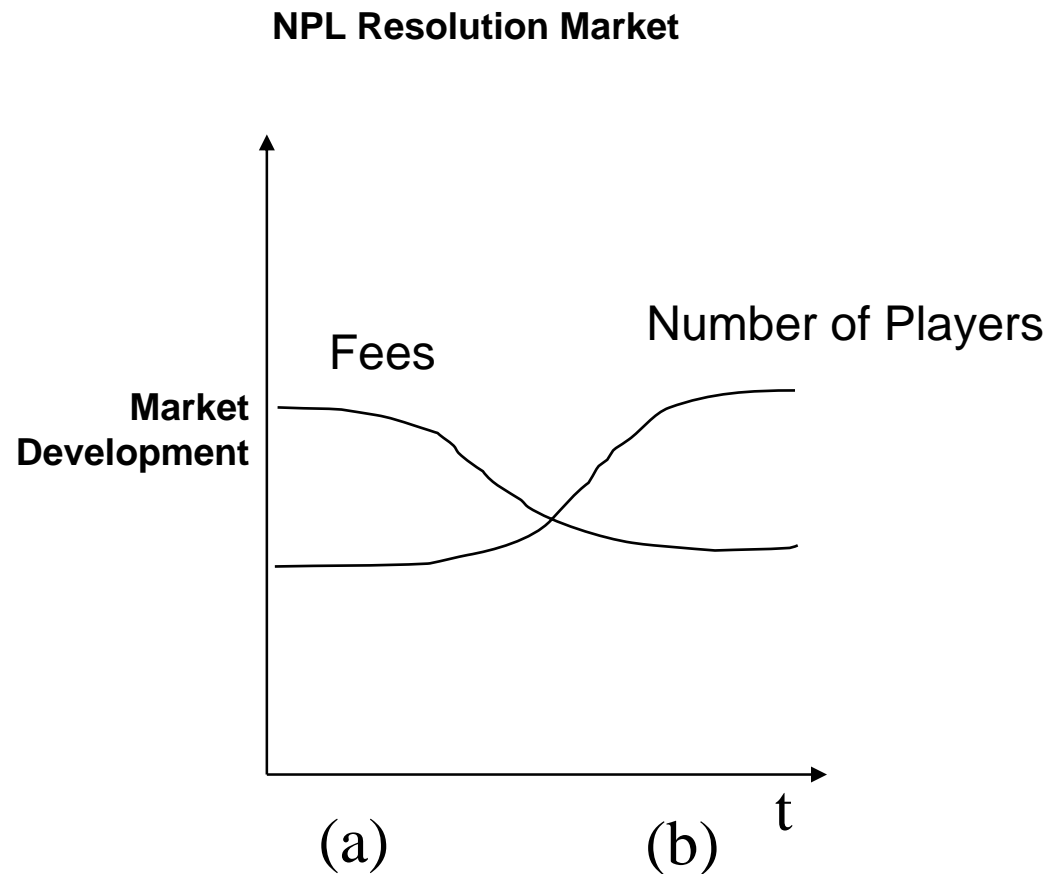
Distressed Debt to Stock Markets



Source: Ernst & Young; Bloomberg

- Value of distressed debt is greater than some local stock markets

NPL Market Development - Asia



NOW

(a) Early Stage: (NOW)

- Few players
- Bigger risks
- High cost for debt & equity

(b) Later Stage

- More players
- Better pricing for seller
- Greater standardization, lower transaction costs
- Still different to project finance market in UK/Europe – became overcrowded

ADB's Involvement: EARLY STAGE

EARLY STAGE: CATALYTIC

- Honest Broker
- Catalyze benchmarks and transparent NPL market
- “Best market practices”
- Catalyzing debt funding from international and domestic banks
- Influence over regulators/State Owned Commercial Banks
- Can provide cross border guarantees
- Fund longer maturities



ADB's Market



Outside ADB Scope:

- South Korea
- Japan
- Taiwan

Tiny

Thailand, Indonesia

Starting

Philippines, Sri Lanka

Expected

India

Up & Running

China

ADB's Role: Overview

MAIN: Senior, limited-recourse debt

- Maximum of 25% of total transaction cost (funding) or US\$ 75 million (whichever is less)
- Full credit, market, asset and legal due diligence
- Market-based spread

(Partial) Credit & Political Risk Guarantees

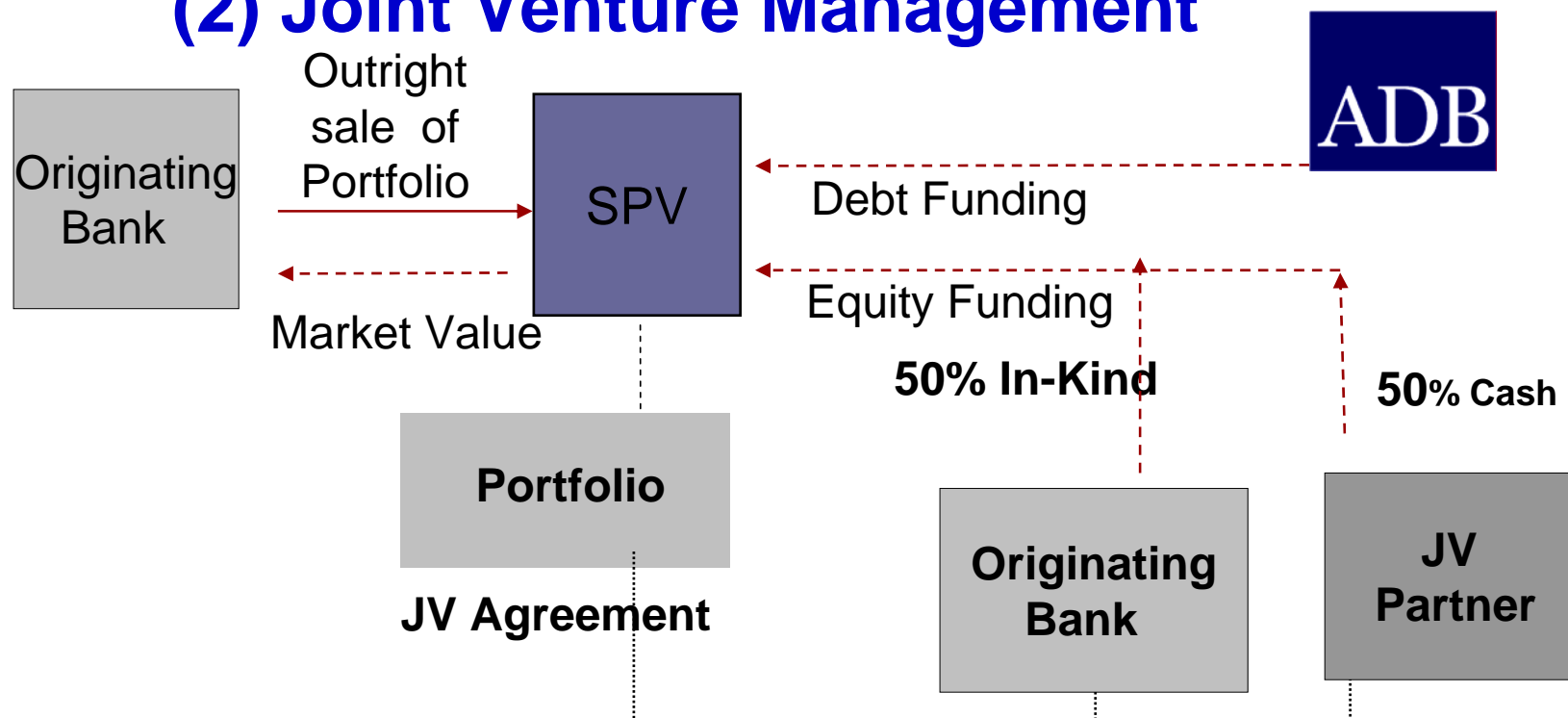
Equity Participation at Early Stage

General “Comfort” as Multilateral Partner/Honest Broker



ADB's role in various structures: (1) Outright Sale

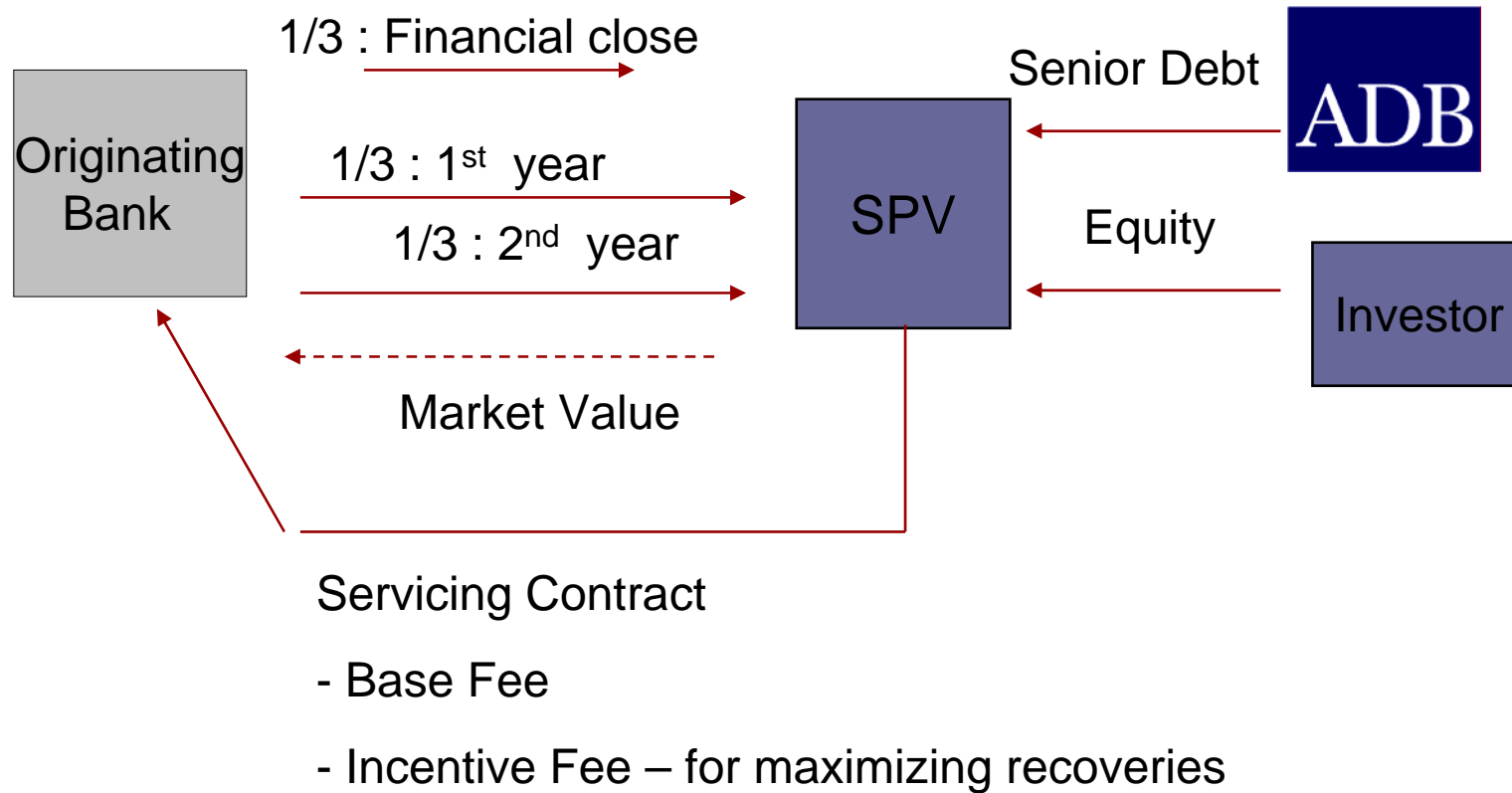
(2) Joint Venture Management



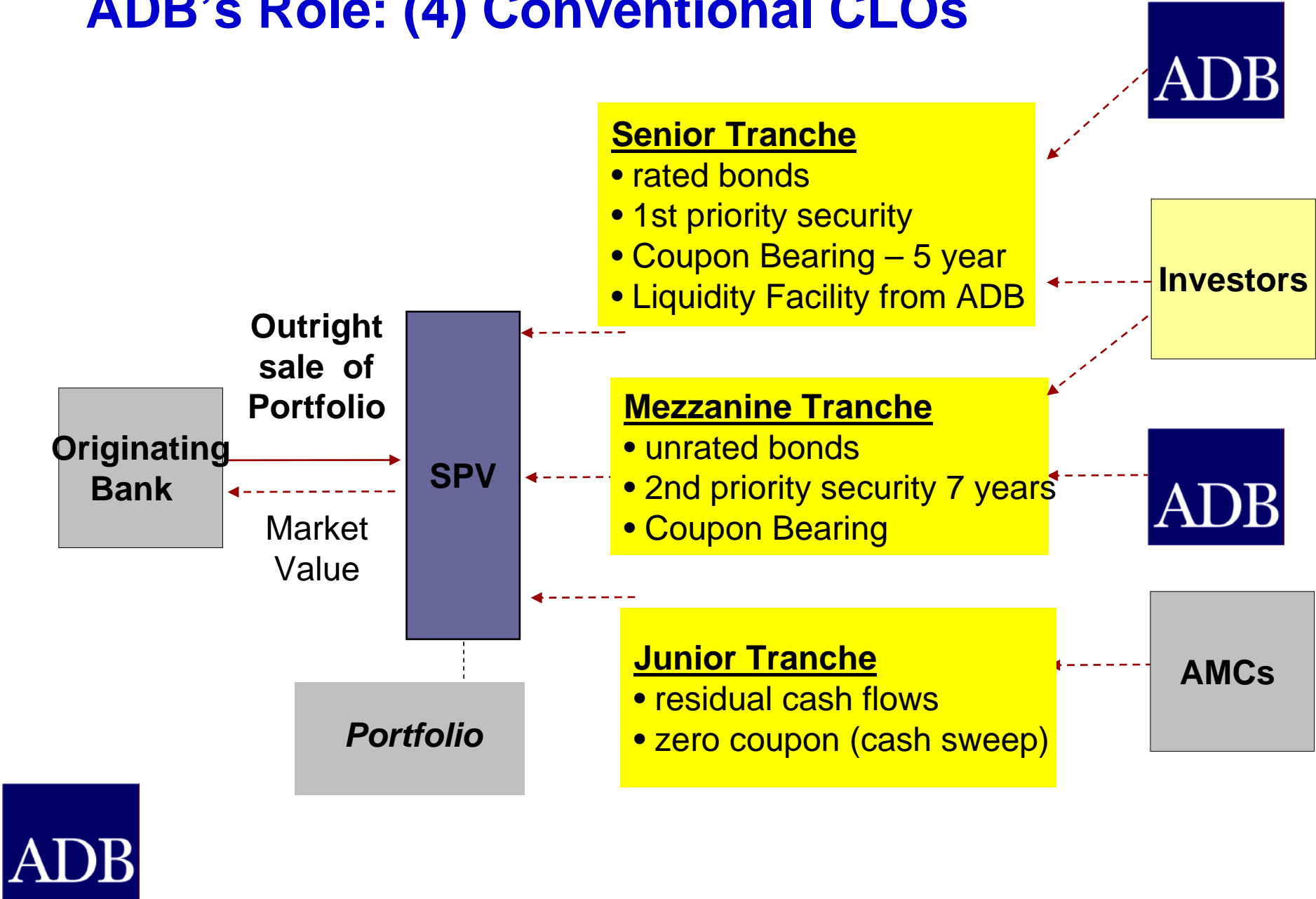
This solution :

- Leverages the expertise & resources of two Partners
- Lower upfront proceeds, Medium up-front write-down
- Easier to negotiate fair value - upside shared with originator.

(3) Synthetic Sale: Seller's objective- defer loss on sale over three years

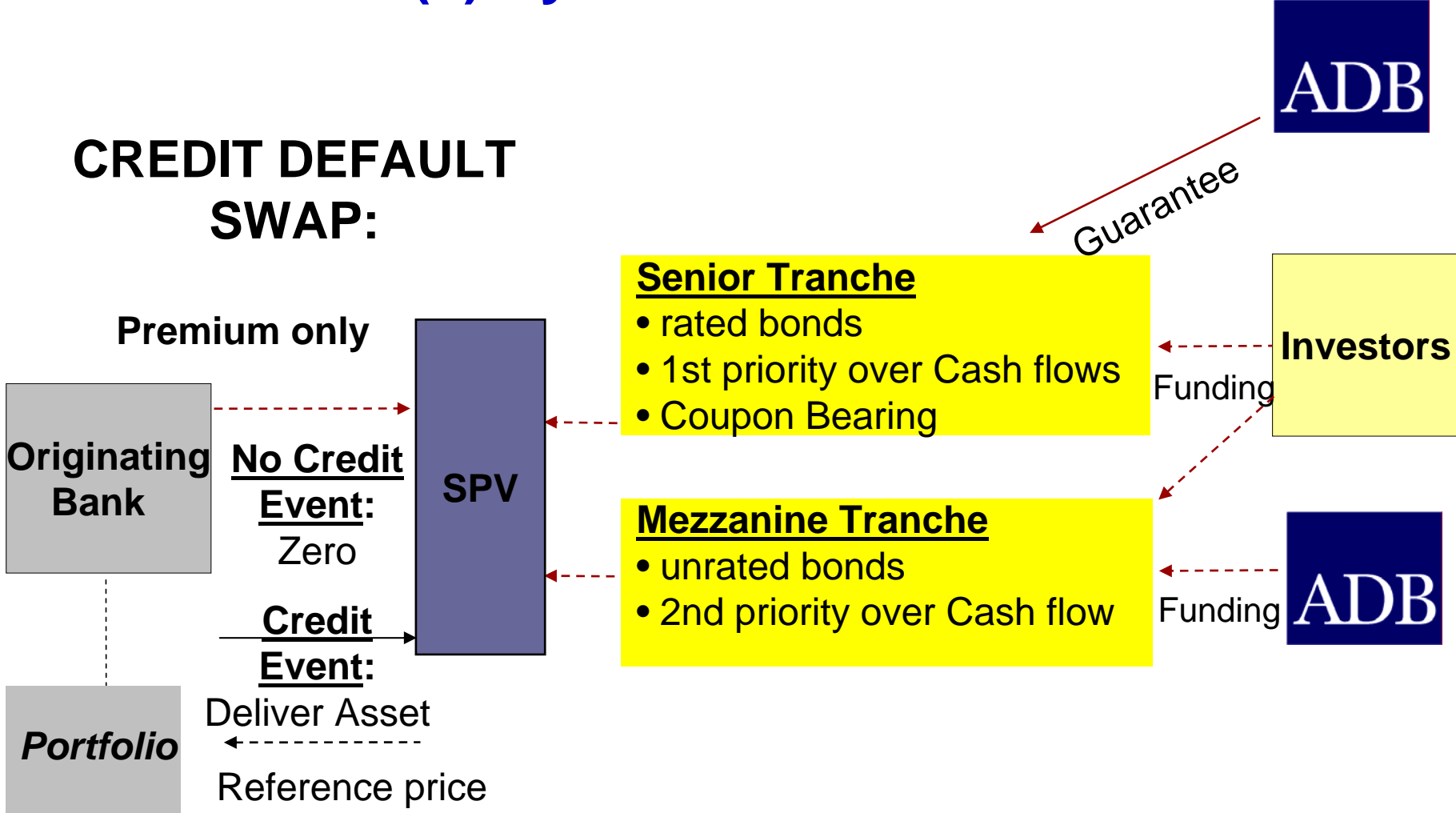


ADB's Role: (4) Conventional CLOs



ADB's Role: (5) Synthetic CLO with CDS

CREDIT DEFAULT SWAP:



Conclusion

INVESTMENT BANKS: Principal business - needs risk sharing

- Require leverage to lower equity cost, (i.e.WACC) & maximize ROE
- Seek diverse partners to better share risks

ASIAN NPL MARKETS: Early-stage

- Fewer players, higher costs
- Limited data on risk-return – track record
- Uncertain regulatory environment, Government influence

ADB: Valuable Early-stage Participant

- Public Sector: Provide political value as multilateral
- Honest Broker –between seller, buyer and regulator
- Private Sector: Offer Debt and Equity funding at riskier early stage



THANK YOU

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