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Private equity

ShoreVest Capital taps into growing global interest in China NPLs

Buyout group eyes $750m from overseas investors for fund targeting mainland bad debt

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YESTERDAY by: Don Weinland in Hong Kong

ShoreVest Capital Partners says it has launched a $750m fund targeting bad debt in China as foreign interest builds in a market known for frustrating outside investors.

The Guangzhou-based firm said it has already raised cash from sovereign wealth funds and pension funds, tapping into still-nascent demand from global investors for non-performing loans in China.

At least three other global investors have moved into the market for China's bad debt this year.

The country's opaque legal system and problems connected to owning state assets have made recovering returns from bad debt in China a complicated task. Some foreign investors that have waded into the market in recent years have found local courts reluctant to allow foreign investors to restructure companies if jobs were at stake.

The level of bad debt in China, however, has surged since 2013, bringing a surplus of NPL deals to the market and adding pressure on Beijing to resolve the problem. Moody's recently downgraded China's sovereign rating for the first time in 25 years in part over concerns regarding surging corporate debt levels.

While the official rate of NPLs at Chinese commercial banks hovers below 2 per cent of total assets, analysts say the true figure could be as high as 15 per cent. ShoreVest estimates that China's stock of bad debt has hit $3tn and the government has incentivised banks to deal with the load.

Global banks started investing in China's bad loans more than a decade ago and several succeeded in striking profitable deals. More recently, the number of transactions pulled off by outsider investors has remained small. At the same time, local distressed debt funds have sprung up, adding some competition at auctions for bad loan portfolios.

Despite the generally tepid sentiment on distressed debt investing in China, ShoreVest says some large global investors are coming around to the market.

"When I raised our first fund 10 years ago, the only LPs [limited partners] interested in Chinese NPLs were those who were open to sophisticated niche strategies," said Benjamin Fanger, ShoreVest managing partner. The asset class has since attracted a wider range of larger global investors, he said.

Last week Bain Capital said it had bought a portfolio of bad loans from a Chinese asset management company for $200m, its first foray into bad debt in China. ShoreVest is acting as the master servicer for the acquisition, according to Bain.

In early 2017, US private equity firm Lone Star and Hong Kong peer PAG began buying non-performing loan portfolios in China, according to several people familiar with the matter, marking the first time in years that new global investors have pushed into the market without a large mainland partner. At the time, PAG said the volume of NPL deals coming on to the market was increasing significantly.

ShoreVest began buying NPL portfolios in China in November. The group was formed by Mr Fanger, a long-time China distressed debt investor, after the split-up of an earlier fund.

Some consultants expressed scepticism on the level of global interest in China's toxic loans and say that, as many investors have long feared, the returns on such investments have continued to fall below expectations.

"I actually don't think it is increasing right now," Ted Osborn, a partner at PwC in Hong Kong, said of the overall sentiment for investments in distressed debt in China. "There are six to eight funds that have dedicated some people to finding deals but they aren't actually finding much. Returns just aren't there at the moment."

Story has been updated to reflect the fact that the ShoreVest Capital fund has not yet closed, and is still raising funds.

Source: https://www.ft.com/content/b00ec5f0-4b47-11e7-a3f4-c742b9791d43?mhq5j=e2