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“The Best Place to Be” (First of a Series)

THE LEAD | November 27, 2019

Earlier this month your correspondent traveled to Tokyo and Seoul, in part to assess how institutional investors view private debt there today.

One highlight was serving on a panel at the Private Debt Investors Forum with several other experienced asset managers. The panel headline was “Global Debt Under the Microscope.” Andrew Hedlund, PDI’s top reporter on the space, moderated.

To an audience comprised mainly of LPs, questions focused on the role of private debt in a diversified portfolio, how an increasingly competitive fundraising and deal making environment is affecting terms and returns, and what to expect in the coming year.

In the Q&A of both this and the other panels of the day, what struck us was the similarity of concerns among Asian investors (and managers) with those in the US and Europe. First and foremost is where we are in the business cycle. The US economy remains in the longest expansion in its history. How long will that last, and what are the consequences of a downturn on private credit?

Then there’s fundraising. Since the virtues of private credit were rediscovered in the aftermath of the credit crisis, money has poured into the asset class. As our *Chart of the Week* shows (courtesy PDI), some 100 firms have raised $112 billion of closed-end funds so far this year. That’s not as heady as levels reached ($239 billion) in 2017, but seems to be on par with last year’s volume of $166 billion.

With all this new demand, aren’t returns going to be squeezed? And isn’t the search for quality deal flow compromised?

Finally, private equity valuations are at all-time highs, as indeed are public equity indices in the US. Doesn’t this represent a bubble similar to what we saw in the tech boom two decades ago, or the buyout binge leading up to the Great Recession? And if so, won’t private credit be negatively impacted when the bubble bursts?

These were the fundamental issues “under the microscope.” They aren’t the same ones managers tackled a couple years ago. Back then, the institutional investor was asking “How do you compare with broadly syndicated loans?” Or “What happens if Libor comes down?” Or worst case, “Can you put my money to work quickly enough?”

But now, with 2019 heading out the door, and 2020 a question mark, uncertainty reigns. “Do you have a work-out person?” and “Where’s the risk premium in private debt?” are more frequently heard. It’s later than you think, is the message.

Yet one leading manager spoke with bracing conviction about the private debt opportunity. “Private debt,” he told the Tokyo audience, “is the best place you can be.”

Why that is will be the subject of our next several issues.